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# Ancillary Relief in Federal Securities Law: A Study in Federal Remedies

George W. Dent Jr.

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# Ancillary Relief in Federal Securities Law: A Study in Federal Remedies

George W. Dent, Jr.\*

## TABLE OF CONTENTS

I. INTRODUCTION .....	866
II. THE HISTORY AND CURRENT PRACTICE OF ANCILLARY RELIEF IN FEDERAL SECURITIES LAW .....	869
III. FEDERAL JUDICIAL REMEDIES AND ANCILLARY RELIEF .....	877
A. ANCILLARY RELIEF IN OTHER AREAS OF ADMINISTRATIVE LAW .....	877
B. FEDERAL EQUITY, STATUTORY INTERPRETATION, AND FEDERAL COMMON LAW .....	882
C. IMPLIED STATUTORY REMEDIES .....	889
IV. THE SCOPE OF THE FEDERAL SECURITIES LAWS .....	899
A. THE TEXT AND LEGISLATIVE HISTORY OF THE FEDERAL SECURITIES LAWS .....	899
1. <i>Express Enforcement Powers</i> .....	899
2. <i>Implied Remedies—The Legislative History             and Purposes of the Federal Securities Laws</i> .....	903
B. RECENT JUDICIAL RESTRICTIONS .....	910
C. THE FEDERAL SECURITIES LAWS AND CORPORATE GOVERNANCE .....	913
1. <i>Federalism and Santa Fe</i> .....	913
2. <i>The Purposes of the Securities Laws, the             Scope of Disclosure, and Corporate             Governance</i> .....	916
V. ANCILLARY RELIEF IN SECURITIES LAW .....	922
A. A GENERAL APPROACH TO ANCILLARY RELIEF ....	923
1. <i>A Blanket Prohibition on Ancillary Relief?</i> ...	923

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2. <i>A Blanket Approval Subject to Judicial Discretion?</i> .....	924
3. <i>Toward a General Approach to Ancillary Relief</i> .....	927
B. ANCILLARY RELIEF IN CONTESTED CASES .....	930
1. <i>Remedies to Rectify Past Violations—Disgorgement, Restitution, Rescission, Sterilization of Voting Rights, Etc.</i> .....	930
2. <i>Relief Pendente Lite</i> .....	933
3. <i>Remedies to Prevent Future Violations—Removal and Appointment of Directors, Appointment of Special Agents and Special Counsel, Etc.</i> .....	933
4. <i>Receiverships</i> .....	941
C. THE SIGNIFICANCE OF THE DEFENDANT'S CONSENT .....	946
VI. THE ALI FEDERAL SECURITIES CODE AND A PROPOSED LEGISLATIVE APPROACH .....	950
VII. CONCLUSION .....	960

## I. INTRODUCTION

The power of federal courts to fashion remedies not expressly provided by federal law has been widely debated. Although the Supreme Court has spoken often in recent years on equitable remedies for constitutional violations<sup>1</sup> and implied damage actions for violations of the federal Constitution<sup>2</sup> and statutes,<sup>3</sup> the Court has not recently dealt with implied equitable remedies under federal statutes. The latter area has attracted much attention,<sup>4</sup> however, especially regarding the

1. See *Swann v. Charlotte-Mecklenburg Bd. of Educ.*, 402 U.S. 1 (1971); *Hill, Constitutional Remedies*, 69 COLUM. L. REV. 1109 (1969); *Nagel, Separation of Powers and the Scope of Federal Equitable Remedies*, 30 STAN. L. REV. 661 (1978).

2. See *Carlson v. Green*, 446 U.S. 14 (1980); *Davis v. Passman*, 442 U.S. 228 (1979); *Butz v. Economou*, 438 U.S. 478 (1978); *Bivens v. Six Unknown Named Agents*, 403 U.S. 388 (1971); *Katz, The Jurisprudence of Remedies: Constitutional Legality and the Law of Torts in Bell v. Hood*, 117 U. PA. L. REV. 1 (1968).

3. See *infra* notes 107-48 and accompanying text.

4. See *Ellsworth, Disgorgement in Securities Fraud Actions Brought by the SEC*, 1977 DUKE L.J. 641; *Farrand, Ancillary Remedies in SEC Civil Enforcement Suits*, 89 HARV. L. REV. 1779 (1976); *Jacobs, Judicial and Administrative Remedies Available to the SEC for Breaches of Rule 10b-5*, 53 ST. JOHN'S L. REV. 397 (1979); *Malley, Far-Reaching Equitable Remedies Under the Securities Acts and the Growth of Federal Corporate Law*, 17 WM. & MARY L. REV. 47 (1975); *Mathews, Recent Trends in SEC Requested Ancillary Relief in SEC Level Injunctive Actions*, 31 BUS. LAW. 1323 (1976); *Sporkin, SEC Developments in Litigation and the Molding of Remedies*, 29 BUS. LAW. 121 (March 1974); *Treadway, SEC Enforcement Techniques: Expanding and Exotic Forms of Ancillary Re-*

Securities and Exchange Commission (the "SEC" or the "Commission"). Over the last fifteen years the SEC has obtained, with increasing frequency and on a scale unprecedented in administrative law, a broad range of equitable remedies—generally known as "ancillary remedies" or "ancillary relief"<sup>5</sup>—not expressly authorized by federal statutes.

Remedies the SEC has obtained against general issuers<sup>6</sup> without express statutory authority include disgorgement of profits, restitution, rescission of transactions, appointment of receivers, sterilization of voting rights, orders to do (or to forbear from doing) acts not otherwise required (or prohibited) by law, and the restructuring of corporate managements by appointing persons to or removing persons from corporate office.<sup>7</sup> Neither the language nor the legislative history of the securities laws expressly empowers the SEC to seek, or the courts to grant, such remedies. The SEC and some commentators have found justification for ancillary relief in the need to effectuate the purposes of the securities laws and in the general equity powers of the federal courts, particularly as reflected in precedents involving other administrative agencies. Nevertheless,

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*lief*, 32 WASH. & LEE L. REV. 637 (1975); Note, *Ancillary Relief in SEC Injunction Suits for Violation of Rule 10b-5*, 79 HARV. L. REV. 656 (1966); Comment, *Court Appointed Directors: Ancillary Relief in Federal Securities Law Enforcement Actions*, 64 GEO. L.J. 737 (1976) [hereinafter cited as Comment, *Court Appointed Directors*]; Comment, *SEC Enforcement of the Rule 10b-5 Duty to Disclose Material Information—Remedies and the Texas Gulf Sulphur Case*, 65 MICH. L. REV. 944 (1967) [hereinafter cited as Comment, *Texas Gulf Sulphur*]; Comment, *Equitable Remedies in SEC Enforcement Actions*, 123 U. PA. L. REV. 1188 (1975) [hereinafter cited as Comment, *Equitable Remedies*]; Comment, *The SEC and Court-Appointed Directors: Time to Tailor the Director to Fit the Suit*, 60 WASH. U.L.Q. 507 (1982) [hereinafter cited as Comment, *Tailor the Director*].

5. The terms "ancillary relief" and "ancillary remedies" are themselves somewhat vague. The word "ancillary" derives from the Latin *ancilla*, meaning a female servant, a handmaiden, WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY (1961), as in the Virgin's response to the angel Gabriel at the Annunciation, "*Ecce ancilla domini*"—"Behold I am the handmaiden of the Lord." *Luke* 1:38. Ancillary relief thus once connoted relief aiding or subsidiary and supplemental to some principal relief to make the principal relief effective. See 1 J. POMEROY, EQUITY JURISPRUDENCE § 171(1) (5th ed. 1941). The term has come to be used more broadly to mean any equitable relief not authorized by statute (note that the titles of many articles cited *supra* note 4 refer to ancillary relief or ancillary remedies), and will be so used in this Article.

6. This Article discusses ancillary remedies against issuers generally and not, except for purposes of comparison, against members of the professional securities industry (such as broker-dealers, securities exchanges, associations of securities dealers, investment companies, and investment advisors). See *infra* notes 161-64 and accompanying text. Treatment of the latter area would raise very different questions.

7. See *infra* notes 10-58 and accompanying text.

close examination of the legislative history raises questions whether certain ancillary remedies promote or hinder the purposes of the securities laws, and recent Supreme Court decisions restricting the federal securities laws and limiting the power of federal courts to imply remedies cast doubts on the courts' power to grant many ancillary remedies.

The American Law Institute's proposed Federal Securities Code attempts to eliminate these uncertainties by authorizing the federal courts "to grant appropriate ancillary or other relief."<sup>8</sup> Although this provision would resolve certain questions, it would also create many new problems of interpretation. More important, the proposed Code offers an opportunity to write a new law of ancillary relief in the securities area and thereby raises the question what that law should be.

The issues raised by ancillary relief in securities law have important implications for administrative law generally. The securities laws typify federal administrative legislation in that they expressly approve certain remedies but neither approve nor deny others. By pursuing novel remedies, the SEC has raised the broader question of when a federal agency and the federal courts may utilize implied remedies. Thus, ancillary relief in securities law offers an interesting study in federal remedies. The Burger Court has begun to redefine the relationship among Congress, federal administrative agencies, and the federal courts.<sup>9</sup> Ancillary relief raises many new questions about these relationships.

After describing the history and current practice of ancillary relief in federal securities law, this Article analyzes the general law of federal remedies and ancillary relief, including ancillary relief in other areas of administrative law, recent developments in federal equity, statutory interpretation, and federal common law, and implied statutory remedies. The Article then examines pertinent aspects of the federal securities laws, including their legislative history and recent judicial interpretations. On this basis the Article recommends both a general approach to ancillary relief in federal securities law and responses to problems of specific remedies. Finally, the Article discusses ancillary relief under the proposed ALI Federal Securities Code and recommends some amendments.

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8. See *infra* text accompanying note 380.

9. See *infra* notes 103-04.

## II. THE HISTORY AND CURRENT PRACTICE OF ANCILLARY RELIEF IN FEDERAL SECURITIES LAW

The most persuasive argument for ancillary relief in federal securities law is that the Supreme Court and many lower courts have approved such relief and that almost no judicial precedent has questioned it.<sup>10</sup> These precedents must be carefully scrutinized, however, to gauge the depth of their support of ancillary relief.

The ancillary remedies that courts have granted in securities law fall roughly into three categories. The first category includes remedies designed to rectify past violations. The most common of these are the equitable monetary remedies of disgorgement and restitution,<sup>11</sup> sometimes accompanied by an ac-

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10. But see *SEC v. American Realty Trust*, 429 F. Supp. 1148 (E.D. Va. 1977), *rev'd*, 586 F.2d 1001 (4th Cir. 1978), in which the district court questioned whether it had power to appoint new board members and held that, even if it did, the power should be reserved for egregious cases because such relief would "infringe on activities traditionally controlled by the states." 429 F. Supp. at 1177-78. The court of appeals reversed the denial of an injunction and, without discussing the issue, instructed the district court to reconsider ancillary relief. 586 F.2d at 1007. See also *SEC v. National Secs., Inc.*, 252 F. Supp. 623, 626 (D. Ariz. 1966) (holding disgorgement not authorized by 1934 Act), *aff'd on other grounds*, 387 F.2d 25 (9th Cir. 1967), *rev'd*, 393 U.S. 453 (1969). Cf. *SEC v. Falstaff Brewing Corp.*, [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,583, at 94,473 (D.D.C. 1978) ("the Court should not, without considerable justification, impose a remedy which would in effect regulate areas traditionally left to internal corporate management"), *aff'd on other grounds*, 629 F.2d 62 (D.C. Cir. 1980).

11. Contested cases include *SEC v. Commonwealth Chem. Secs. Corp.*, 574 F.2d 90 (2d Cir. 1978); *SEC v. Galaxy Foods, Inc.*, 556 F.2d 559 (2d Cir. 1977); *SEC v. Shapiro*, 494 F.2d 1301 (2d Cir. 1974); *Chris-Craft Indus., Inc. v. Piper Aircraft Corp.*, 480 F.2d 341, 390-92 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973); *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1103-06 (2d Cir. 1972); *SEC v. Dimensional Entertainment Corp.*, 493 F. Supp. 1270, 1279 (S.D.N.Y. 1980); *SEC v. Penn Central Co.*, 425 F. Supp. 593, 599 (E.D. Pa. 1976) (motion to dismiss claim for disgorgement denied); *SEC v. Jet Travel Serv. Inc.*, [1975-76 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,317, at 98,609 (M.D. Fla. 1975); *SEC v. Blatt*, [1975-76 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,281, at 98,444 (S.D. Fla. 1975); *SEC v. Weisberger*, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,108, at 97,944 (S.D.N.Y. 1975); *SEC v. R.J. Allen & Assocs., Inc.*, 386 F. Supp. 866, 881 (S.D. Fla. 1974); *SEC v. Golconda Mining Co.*, 327 F. Supp. 257, 260 (S.D.N.Y. 1971); *SEC v. Wong*, 252 F. Supp. 608, 613 (D.P.R. 1966). See generally Ellsworth, *supra* note 4 (discussing the role of disgorgement in the SEC's enforcement program).

The first contested case in which the SEC sought disgorgement was *SEC v. Texas Gulf Sulphur Co.*, 258 F. Supp. 262 (S.D.N.Y. 1966), *modified*, 401 F.2d 883 (2d Cir. 1968), *cert. denied*, 394 U.S. 976 (1969). 3B H. BLOOMENTHAL, *SECURITIES AND FEDERAL CORPORATE LAW* § 11.25, at 11-132 (1980); Comment, *Texas Gulf Sulphur*, *supra* note 4, at 945. Prior to *Texas Gulf Sulphur* the SEC had obtained such relief only by consent and in contested cases had sought no ancillary relief other than the appointment of a receiver. Ellsworth, *supra* note 4, at

counting.<sup>12</sup> If an illegal transaction remains unconsummated, a court may order a defendant to rescind or to offer to rescind the transaction.<sup>13</sup> Some provisions of the securities laws clearly contemplate such relief.<sup>14</sup> Courts have also granted these remedies to deter future violations by depriving defendants of their wrongful profits.<sup>15</sup> To prevent defendants from profiting from their violations, courts may enjoin them from voting, or order them to divest themselves of, stock they illegally acquired.<sup>16</sup> Defendants may be ordered to perform properly any required act which they performed improperly or failed to perform.<sup>17</sup>

A second category comprises remedies designed "to preserve the status quo pending final determination of the questions raised."<sup>18</sup> These include a freeze on assets,<sup>19</sup> certain

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641 & n.1, 643-47. There have also been many consent decrees ordering such relief. See Jacobs, *supra* note 4, at 413-17, 437-39, 445-46 (citing cases).

12. Contested cases include SEC v. Western Pacific Gold & Silver Exch. Corp., [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,064, at 97,734 (D. Nev. 1975); SEC v. R.J. Allen & Assocs., Inc., 386 F. Supp. 866, 880 (S.D. Fla. 1974); SEC v. Wong, 252 F. Supp. 608, 614 (D. P.R. 1966); SEC v. Gulf Intercont. Fin. Corp., 223 F. Supp. 987, 996 (S.D. Fla. 1963); Kardon v. National Gypsum Co., 73 F. Supp. 798, 802 (E.D. Pa. 1947).

13. Contested cases include Wright v. Heizer Corp., 560 F.2d 236, 252 (7th Cir. 1977); Chris-Craft Indus., Inc. v. Piper Aircraft Corp., 480 F.2d 341, 390 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973); SEC v. Texas Gulf Sulphur Co., 446 F.2d 1301, 1309 (2d Cir. 1971), *cert. denied*, 404 U.S. 1005 (1972); SEC v. Weisberger, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,108, at 97,944 (S.D.N.Y. 1975). See Mills v. Electric Auto-Lite Co., 396 U.S. 375, 386 (1970) (remedies could include "setting aside" a merger). As in Deckert v. Independence Shares Corp., 311 U.S. 282 (1940), discussed *infra* notes 44-52 and accompanying text, in most private suits disgorgement, restitution, or rescission will not be ancillary to an injunction but will be the principal relief sought. There have also been many consent decrees ordering such relief. See Mathews, *supra* note 4, at 1336 (citing cases).

14. See *infra* text following note 46.

15. See SEC v. Texas Gulf Sulphur Co., 258 F. Supp. 262 (S.D.N.Y. 1966), *modified*, 401 F.2d 883 (2d Cir. 1968), *cert. denied*, 394 U.S. 976 (1969).

16. Contested cases include Chris-Craft Indus., Inc. v. Piper Aircraft Corp., 480 F.2d 341, 380 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973); SEC v. Falstaff Brewing Co., [1977-78 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,117, at 92,023 (D.D.C. 1977); SEC v. General Refractories Co., 400 F. Supp. 1248, 1259 (D.D.C. 1975); SEC v. Techni-Culture, Inc., [1973-74 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,501, at 95,759 (D. Ariz. 1974). There have also been many consent decrees ordering such relief. See cases cited in Jacobs, *supra* note 4, at 447-48; Mathews, *supra* note 4, at 1337.

17. For example, a defendant may be ordered to file a corrected document with the SEC or to resolicit proxies. See SEC v. Parklane Hosiery Co., 422 F. Supp. 477, 487 (S.D.N.Y. 1976), *aff'd*, 558 F.2d 1083 (2d Cir. 1977); SEC v. Beisinger Indus. Corp., 421 F. Supp. 691, 696 (D. Mass. 1976), *aff'd*, 552 F.2d 15 (1st Cir. 1977).

18. Deckert v. Independence Shares Corp., 311 U.S. 282, 290 (1940) (discussed *infra* notes 44-52 and accompanying text).

19. See Deckert v. Independence Shares Corp., 311 U.S. 282, 290 (1940); SEC v. Manor Nursing Centers, Inc., 458 F.2d 1082, 1105 (2d Cir. 1972); Los An-

types of injunctions *pendente lite*,<sup>20</sup> and the appointment of a receiver to preserve property during litigation and to distribute the property pursuant to a final judgment.<sup>21</sup>

The third category encompasses remedies designed to discourage future violations through regulation of the defendant's future behavior that goes beyond merely enjoining violations of the securities laws. Such regulation may take either of two forms. First, the defendant may be ordered to perform (or to refrain from performing) specified acts not otherwise required (or forbidden) by law.<sup>22</sup> Second, the court may change corporate management by appointing persons to, or removing incumbents from, managerial positions. Judicial support in contested cases for this second type of remedy is extremely tenuous;

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geles Trust Deed & Mortgage Exch. v. SEC, 264 F.2d 199, 213 (9th Cir. 1959); SEC v. National Farmers Org., Inc., 7 S.E.C. Doc. 603 (S.D. Iowa 1975). Cf. SEC v. American Inst. Counselors, Inc., [1975-76 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,388, at 98,963 (D.D.C. 1975) (Investment Company Act case).

20. See SEC v. Western Pacific Gold & Silver Exch. Corp., [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,064, at 97,734 (D. Nev. 1975) (injunction against altering, destroying, or concealing various corporate documents and assets); SEC v. Fifth Avenue Coach Lines, Inc., 289 F. Supp. 3, 4 (S.D.N.Y. 1968), *aff'd*, 435 F.2d 510 (2d Cir. 1970) (injunction pending trial against entering into certain transactions (by consent) or making certain withdrawals (contested)).

21. SEC v. United Fin. Group, Inc., 474 F.2d 354, 358 (9th Cir. 1973); SEC v. Koenig, 469 F.2d 198, 202 (2d Cir. 1972); Los Angeles Trust Deed & Mortgage Exch. v. SEC, 285 F.2d 162, 181 (9th Cir. 1960), *cert. denied*, 366 U.S. 919 (1961); SEC v. Gulf Intercont. Fin. Corp., 223 F. Supp. 987, 996 (S.D. Fla. 1963).

For decisions reversing the denial of a receivership and remanding, see Deckert v. Independence Shares Corp., 311 U.S. 282 (1940); SEC v. Bowler, 427 F.2d 190, 198 (4th Cir. 1970). There have been many appointments of receivers over broker-dealers. See SEC v. Investors Sec. Corp., 560 F.2d 561, 563 (3d Cir. 1977); SEC v. Charles Plohn & Co., 433 F.2d 376, 379 (2d Cir. 1970); Lankenau v. Coggeshall & Hicks, 350 F.2d 61, 63 (2d Cir. 1965); SEC v. R.J. Allen & Assocs., Inc., 386 F. Supp. 866, 879 (S.D. Fla. 1974); SEC v. H.S. Simmons & Co., 190 F. Supp. 432, 433 (S.D.N.Y. 1961). But see SEC v. Buongiorno, [1964-66 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 91,499 (S.D.N.Y. 1965) (denial of receiver).

22. Such orders have ranged from commanding a corporation to keep additional records to prohibiting a corporation from acquiring other companies or entering any new line of business without court approval. Contested cases include Wright v. Heizer Corp., 560 F.2d 236, 256 (7th Cir. 1977) (order to make additional disclosure, modify loan agreements, and forbid corporate securities transactions unless approved by shareholders or court); SEC v. Heritage Trust Co., 402 F. Supp. 744, 752 (D. Ariz. 1975) (order to give SEC access to corporate books to monitor compliance with law); SEC v. General Refractories Co., 400 F. Supp. 1248, 1262 (D.D.C. 1975) (injunction against buying or selling stock of a company); SEC v. Techni-Culture, Inc., [1973-74 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,501, at 95,759 (D. Ariz. 1974) (order to surrender certain stock and to report stock holdings and any changes therein to court). A case involving a consent decree is SEC v. Holiday Magic, Inc., Civil No. C-73-1095 (N.D. Cal. Apr. 2, 1974) (prohibiting corporation from selling securities in certain circumstances or "expand[ing] their operations to a new product line or business" without approval of special counsel). See also Mathews, *supra* note 4, at 1337 (citing cases).



nearly all such relief has been granted in consent decrees.<sup>23</sup> Indeed, until recently the Commission rarely even requested this type of remedy.<sup>24</sup> Only in the last few years has the SEC begun arguing in many cases that an injunction against violations cannot by itself ensure compliance.<sup>25</sup> The Commission has professed concern, however, that a receivership might damage creditors and investors—the very persons the SEC is supposed to protect.<sup>26</sup> The Commission, therefore, has begun seeking changes in corporate management without the appointment of a receiver. These changes include appointing a special agent to conduct an investigation<sup>27</sup> or to oversee disclosure,<sup>28</sup> and ousting several directors and court appointment of a majority of directors with the approval of the SEC.<sup>29</sup>

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23. Although some courts have appointed special agents or special counsel in contested cases, see *infra* note 27, none has restructured a corporate board in a contested case. See *infra* note 29.

24. See Sommer, *The Impact of the SEC on Corporate Governance*, 41 LAW & CONTEMP. PROBS. 115, 128 (Summer 1977) ("At one time the Commission typically sought only conventional injunctive relief."). For example, in *In re Franchard Corp.*, [1964-66 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 77,113, at 82,046 (1964), the Commission conceded its lack of power "to define federal standards of directors' responsibility in the ordinary operations of business enterprises." See *infra* text accompanying notes 246-47.

25. See Sommer, *supra* note 24, at 128 ("[I]n recent years [the Commission] has increasingly tried to expand the . . . relief resulting from civil court proceedings, a response perhaps to the criticism that the typical result of its civil proceedings has been only a slap on the wrist."); Sporkin, *supra* note 4, at 122 ("[W]e [the SEC] have been trying more and more to structure our remedies to fit the particular fact pattern presented."); Comment, *Texas Gulf Sulphur*, *supra* note 4, at 963 ("the SEC believes that an injunction without more is not a sufficient remedy"). See also Hazen, *Administrative Enforcement: An Evaluation of the Securities and Exchange Commission's Use of Injunctions and Other Enforcement Methods*, 31 HASTINGS L.J. 427, 445 (1979) ("the simple injunction has little deterrent effect").

26. See Sporkin, *supra* note 4, at 123. Cf. *infra* note 341 and accompanying text (SEC has argued that since it can obtain a receiver and since other remedies affecting corporate governance are not as drastic as the receivership, a fortiori it can obtain such other remedies, and with a lesser showing).

27. SEC v. Beisinger Indus. Corp., 552 F.2d 15 (1st Cir. 1977), *aff'd* 421 F. Supp. 691 (D. Mass. 1976) (special agent appointed to bring corporation into compliance with securities laws, with district court specifying several tasks); SEC v. Koenig, 469 F.2d 198, 202 (2d Cir. 1972) (limited receiver appointed to conduct an investigation, file reports, and hold a shareholders' meeting); SEC v. Western Geothermal & Power Corp., [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,920 (D. Ariz. 1979) (special officer appointed to insure compliance with securities laws). But see SEC v. Parklane Hosiery Co., 422 F. Supp. 477 (S.D.N.Y. 1976), *aff'd*, 558 F.2d 1083 (2d Cir. 1977) (court denied request for appointment of special counsel).

28. See generally *supra* note 27.

29. No court has removed or appointed directors or officers in a contested case, although the issue has arisen indirectly in a few cases. See *Handler v. SEC*, 610 F.2d 656 (9th Cir. 1979) (rejecting collateral attack on consent decree in *Mattel*, discussed *infra* notes 30-40 and accompanying text); SEC v. Lincoln

The most publicized decision involving such corporate governance reforms, *SEC v. Mattel, Inc.*,<sup>30</sup> typifies such cases. In its initial complaint, the SEC alleged that in 1973 Mattel made filings and press releases that were false and misleading.<sup>31</sup> Simultaneously with the filing of the complaint, Mattel consented to, and the court entered, a judgment that permanently enjoined Mattel from violating the 1934 Act. The judgment also required Mattel to appoint two new unaffiliated directors<sup>32</sup> and to establish an audit committee<sup>33</sup> and a "Litigation and Claims Committee,"<sup>34</sup> each with specified powers. The Commission obtained the relief "to avoid repetition of the alleged violations."<sup>35</sup> When Mattel informed the SEC a few months later of further securities law violations, the Commission obtained Mattel's consent to additional relief, including the appointment and maintenance for five years of a majority of unaffiliated directors on a new executive committee and on the whole board, the correction of false filings, and the selection by the unaffiliated directors of a special counsel to investigate and bring suits for securities law violations and to select a special auditor to audit certain financial statements.<sup>36</sup> Despite initial reluctance, the district judge granted the requested relief with certain modifications.<sup>37</sup> The company and the SEC enforcement staff chose

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Thrift Ass'n, 557 F.2d 1274 (9th Cir. 1977) (court of appeals notes that district court had appointed a board of trustees to replace a receiver); *International Controls Corp. v. Vesco*, 490 F.2d 1334 (2d Cir.), *cert. denied*, 417 U.S. 932 (1974) (rejecting collateral attack on consent decree providing for court-appointed special counsel and board of directors). For other consent decrees, see cases cited in Mathews, *supra* note 4, at 1334-35, 1340-42, 1345-52.

30. 4 S.E.C. Doc. 724, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,754 (D.D.C. 1974).

31. *Id.* The complaint alleged that in 1973 Mattel made false and misleading filings and press releases by overstating its profits, understating its costs, and using deceptive accounting procedures.

32. To accomplish this the SEC also forced an increase in the number of directors provided in Mattel's by-laws. See Malley, *supra* note 4, at 56.

33. 4 S.E.C. Doc. 724, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,754 (D.D.C. 1974). The Financial Controls and Audit Committee was to oversee accounting procedures and controls, review financial reports and press releases, determine the corporate position in any disagreement with the corporation's auditors, and review any proposed change of independent auditors.

34. *Id.* The committee was to control litigation against insiders, and review conflicts of interest and establish corporate policies with regard to such matters. The two new directors and the members of the two new committees were to be acceptable to the court and the Commission.

35. 4 S.E.C. Doc. 724, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,754, at 96,486.

36. *SEC v. Mattel, Inc.*, 5 S.E.C. Doc. 241, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,807 (D.D.C. 1974). The unaffiliated directors were to be appointed with court approval.

37. See Mathews, *supra* note 4, at 1328.

new directors from a list of persons cleared by the Commission.<sup>38</sup> Shareholders played no role in this selection and were denied their usual right to fill these directorships during the five-year period of the decree.<sup>39</sup> The judgment involved substantial, continuing court involvement in the corporation's affairs.<sup>40</sup>

Most ancillary remedies have been obtained ancillary to an injunction in an SEC enforcement proceeding. On occasion, however, the SEC has secured ancillary relief in an administrative proceeding<sup>41</sup> or in a civil suit in which no injunction was granted.<sup>42</sup> Private plaintiffs also have occasionally obtained ancillary relief.<sup>43</sup>

The only Supreme Court case dealing with ancillary relief

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38. See Loo, *The SEC's Role in Director Selection*, in DUTIES AND RESPONSIBILITIES OF OUTSIDE DIRECTORS 77, 98 (A. Cohen & R. Loeb eds. 1978).

39. There is no mention of shareholders in the decree, and presumably the decree supersedes state laws providing for shareholder election of directors. See *International Controls Corp. v. Vesco*, 490 F.2d 1334 (2d Cir.), cert. denied, 417 U.S. 932 (1974).

40. In addition to the usual judicial functions in supervising an injunction, the decree contemplated court approval of new directors, receipt of reports of the special counsel and special auditor, determination of special auditor's compensation, resolution of disputes between the special counsel and the board of directors, and receipt of requests for instructions from the special auditor. 5 S.E.C. Doc. 241, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,807 (D.D.C. 1974).

41. Since the SEC can generally bring administrative proceedings only against securities professionals (e.g., broker-dealers and investment companies) and other professionals (principally lawyers and accountants), ancillary relief in administrative proceedings has been obtained primarily against such persons, and by consent. See Mathews, *Litigation and Settlement of SEC Administrative Enforcement Proceedings*, 29 CATH. U. L. REV. 215, 230-31 & n.62 (1980). Ancillary relief has been obtained in rule 2(e) proceedings. See Treadway, *supra* note 4, at 667-76. Sometimes ancillary relief is obtained indirectly, as when the SEC orders that a broker's registration be revoked unless the principal individual offender (who could not be subjected to administrative proceedings) is disassociated from the broker. See Jacobs, *supra* note 4, at 425.

42. *Chris-Craft Indus., Inc. v. Piper Aircraft Corp.*, 480 F.2d 341, 390-91 (2d Cir.), cert. denied, 414 U.S. 910 (1973); *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1100, 1104 (2d Cir. 1972).

43. *Deckert v. Independence Shares Corp.*, 311 U.S. 282 (1940) (discussed *infra* notes 44-52 and accompanying text); *Wright v. Heizer Corp.*, 560 F.2d 236, 252-58 (7th Cir. 1976) (special injunction entered); *Kohn v. American Metal Climax, Inc.*, 322 F. Supp. 1331, 1336 (E.D. Pa. 1970) (defendant ordered to make registered public offering); *Braasch v. Muscat*, [1967-69 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 92,148 (S.D.N.Y.), remanded on other grounds, 398 F.2d 1022 (2d Cir. 1968) (special fiscal agent appointed); *Kardon v. National Gypsum Co.*, 73 F. Supp. 798, 803 (E.D. Pa. 1947) (accounting ordered). Receivers have recovered ancillary relief in some cases. See, e.g., *Lankenau v. Coggeshall & Hicks*, 350 F.2d 61, 63-67 (2d Cir. 1965); *Esbitt v. Dutch-American Mercantile Corp.*, 335 F.2d 141, 142-43 (2d Cir. 1964).

in securities law is *Deckert v. Independence Shares Corp.*<sup>44</sup> The plaintiffs there sued under section 12(2) of the Securities Act of 1933<sup>45</sup> and sought rescission and restitution, a receiver to settle claims against the issuer and to wind up its business, and an injunction restraining a trustee from disposing of assets of the trust.<sup>46</sup> The Supreme Court, reversing the court of appeals, held that a suit could be maintained and an injunction entered against the trustee.<sup>47</sup> Although the issue on appeal was the susceptibility of the trustee to suit rather than the availability of ancillary relief, the Court stated in dictum that further equitable relief could be granted on two grounds. First, section 12(2) states that the purchaser "may sue either in law or in equity . . . to recover the consideration paid." The statute could hardly be clearer in authorizing rescission or restitution, "at least where there are circumstances making the legal remedy inadequate."<sup>48</sup> Piling dictum on dictum, the Court also cited section 22(a), which grants courts jurisdiction "of all suits in equity and actions at law brought to enforce any liability or duty created by" the 1933 Act, and stated:

The power to *enforce* implies the power to make effective the right of recovery afforded by the Act. And the power to make the right of recovery effective implies the power to utilize any of the procedures or actions normally available to the litigant according to the exigencies of the particular case.<sup>49</sup>

In *Deckert* restitution and rescission were the principle relief sought rather than ancillary relief,<sup>50</sup> and these remedies were not implied, but were within the language of the statute. The Court's holding is not necessarily relevant to the SEC which, because it is never a purchaser, cannot sue under section 12(2). The Court's other basis—section 22(a)—is not only dictum but is also ambiguous. In *Deckert* the plaintiffs sought

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44. 311 U.S. 282 (1940).

45. 15 U.S.C. § 771(2) (1976). Section 12(2) permits a private action by a buyer of securities against one who "offers or sells" by means of false or misleading statements or omissions of material facts.

46. 311 U.S. at 285.

47. The opinion's reasoning is surprisingly opaque. The Court stated that "the injunction was a reasonable measure to preserve the status quo pending final determination of the questions raised by the bill," *id.* at 290, that "the complicated arrangement between [the trustee and the issuer] might make it extremely difficult to obtain satisfaction of any claim established against" the issuer, *id.* at 289, and that part of the consideration paid by plaintiffs was held by the trustee, *id.* The Court did not, however, state which of these facts was essential to maintenance of the suit.

48. *Id.* at 289.

49. *Id.* at 288 (emphasis in original).

50. See *supra* note 5 as to the meaning of "ancillary relief."

an injunction and a receiver solely to maintain the status quo pending final disposition of the case so as to prevent a dissipation of assets that could have made a final judgment in their favor meaningless. The Court may have intended to approve only this limited ancillary relief, or it may have intended a much broader approval of ancillary remedies. Most important, recent Supreme Court decisions have rejected reliance on jurisdictional provisions like section 22(a) as a source of remedial power.<sup>51</sup> It may have been relevant to the decision, though it was not mentioned as such, that the defendant was an investment company.<sup>52</sup>

Thus *Deckert*, the Supreme Court's only encounter with ancillary relief in securities law, provides only shaky authority for most ancillary relief. Nonetheless, lower federal courts have often approved this type of remedy. In addition to citing *Deckert*<sup>53</sup> and following its reliance on provisions granting jurisdiction,<sup>54</sup> these lower courts have grounded their decisions principally on the general equity powers of federal tribunals.<sup>55</sup> The courts have also stressed other factors, including the need to effectuate the purposes and improve the enforcement of the securities laws,<sup>56</sup> and have cited cases granting ancillary relief

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51. See *infra* notes 121-22 and accompanying text.

52. Although the facts of the case arose before enactment of the Investment Company Act of 1940, the Act had been enacted when the Court decided *Deckert*. The abuses of investment companies and their need for regulation were widely acknowledged at the time and may have led the Court to use broader language than it would have for a company not in the securities industry.

53. See *SEC v. Investors Sec. Corp.*, 560 F.2d 561, 567 (3d Cir. 1977); *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1103 (2d Cir. 1972); *Los Angeles Trust Deed & Mortgage Exch. v. SEC*, 285 F.2d 162, 181 (9th Cir. 1960), *cert. denied*, 366 U.S. 919 (1961); *SEC v. Transamerica Corp.*, 163 F.2d 511, 518 (3d Cir. 1947); *SEC v. R.J. Allen & Assocs., Inc.*, 386 F. Supp. 866, 881 (S.D. Fla. 1974).

54. See *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1103 (2d Cir. 1972); *SEC v. Texas Gulf Sulphur Co.*, 446 F.2d 1301, 1308 (2d Cir. 1971), *cert. denied*, 404 U.S. 1005 (1972); *Los Angeles Trust Deed & Mortgage Exch. v. SEC*, 285 F.2d 162, 181 (9th Cir. 1960), *cert. denied*, 366 U.S. 919 (1961); *SEC v. R.J. Allen & Assocs., Inc.*, 386 F. Supp. 866, 880-81 (S.D. Fla. 1974).

55. See *infra* note 78.

56. See *Chris-Craft Indus., Inc. v. Piper Aircraft Corp.*, 480 F.2d 341, 390-91 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973); *SEC v. Texas Gulf Sulphur Co.*, 446 F.2d 1301, 1308 (2d Cir. 1971), *cert. denied*, 404 U.S. 1005 (1972); *SEC v. Dimensional Entertainment Corp.*, 493 F. Supp. 1270, 1279 (S.D.N.Y. 1980); *SEC v. Beisinger Indus. Corp.*, 421 F. Supp. 691 (D. Mass. 1976), *aff'd*, 552 F.2d 15, 18-19 (1st Cir. 1977); *SEC v. Commonwealth Chem. Secs., Inc.*, [1975-76 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,495 (S.D.N.Y. 1976), *modified on other grounds*, 574 F.2d 90, 95-96 (2d Cir. 1978); *SEC v. Weisberger*, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,108 (S.D.N.Y. 1975); *SEC v. R.J. Allen & Assocs., Inc.*, 386 F. Supp. 866, 881 (S.D. Fla. 1974); *SEC v. Shapiro*, 349 F. Supp. 46 (S.D.N.Y. 1972), *aff'd*, 494 F.2d 1301, 1309 (2d Cir. 1974); *SEC v. Wong*, 252 F.

in other areas of administrative law,<sup>57</sup> and Supreme Court cases implying private damage actions.<sup>58</sup> The next two Parts of this Article describe and analyze these justifications.

### III. FEDERAL JUDICIAL REMEDIES AND ANCILLARY RELIEF

Cases approving ancillary relief in securities law have relied on the general equitable power of federal courts to fashion remedies to enforce federal statutes, citing many federal administrative cases granting ancillary relief and cases implying private rights of action. This Part reviews the remedial powers of federal courts, the law of ancillary relief, and some recent trends in these areas.

#### A. ANCILLARY RELIEF IN OTHER AREAS OF ADMINISTRATIVE LAW

There is no general statutory authority for federal courts to grant ancillary relief.<sup>59</sup> In the oft-cited case of *Porter v. Warner Holding Co.*,<sup>60</sup> however, the Supreme Court stated that

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Supp. 608, 611-14 (D.P.R. 1966). Similarly, several courts have stressed the deterrent function of ancillary relief. See *SEC v. Shapiro*, 494 F.2d 1301, 1308 (2d Cir. 1974); *Chris-Craft Indus., Inc. v. Piper Aircraft Corp.*, 480 F.2d 341, 391 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973); *SEC v. Dimensional Entertainment Corp.*, 493 F. Supp. 1270, 1279 (S.D.N.Y. 1980); *SEC v. Galaxy Foods, Inc.*, 417 F. Supp. 1225, 1249 (E.D.N.Y. 1976), *aff'd*, 556 F.2d 559 (2d Cir. 1977).

57. *See Handler v. SEC*, 610 F.2d 656, 659 (9th Cir. 1979); *Chris-Craft Indus., Inc. v. Piper Aircraft Corp.*, 480 F.2d 341, 391 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973); *SEC v. Radio Hill Mines Co.*, 479 F.2d 4 (2d Cir. 1973); *SEC v. Texas Gulf Sulphur Co.*, 446 F.2d 1301, 1308 (2d Cir. 1971), *cert. denied*, 404 U.S. 1005 (1972); *Los Angeles Trust Deed & Mortgage Exch. v. SEC*, 285 F.2d 162, 180-81 (9th Cir. 1960), *cert. denied*, 366 U.S. 919 (1961); *SEC v. Wong*, 252 F. Supp. 608, 611-14 (D.P.R. 1966); *SEC v. H.S. Simmons & Co.*, 190 F. Supp. 432, 432-33 (S.D.N.Y. 1961). See 3 L. LOSS, *SECURITIES REGULATION* 1827-29 (2d Ed. 1961).

58. See *infra* notes 107-08 and accompanying text.

59. The All Writs Act, 28 U.S.C. § 1651(a) (1976), which permits federal courts to "issue all writs necessary or appropriate in aid of their respective jurisdictions and agreeable to the usages and principles of law," authorizes writs "to preserve the *status quo* while administrative proceedings are in progress and prevent the impairment of the effective exercise of appellate jurisdiction." *FTC v. Dean Foods Co.*, 384 U.S. 597, 604 (1966) (approving a preliminary injunction against consummation of a merger pending determination of its legality). A court may not use the act to enjoin action that is not detrimental to its jurisdiction. *Calloway v. Benton*, 336 U.S. 132, 149-51 (1949). The Act is a means of avoiding inflexible application of the final judgment rule. See 9 J. MOORE, *FEDERAL PRACTICE* ¶ 110.26, at 276 (1983). Moreover, even for the purpose of protecting court jurisdiction the Act is limited to writs "agreeable to the usages and principles of law," and therefore has been held not to authorize an interlocutory injunction for which there was no precedent. *De Beers Consol. Mines v. United States*, 325 U.S. 212, 219, 222-23 (1945).

60. 328 U.S. 395 (1946).

"[u]nless otherwise provided by statute, all the inherent equitable powers of the District Court are available . . . . Moreover, the comprehensiveness of this equitable jurisdiction is not to be denied or limited in the absence of a clear and valid legislative command."<sup>61</sup> The relevant statute in *Porter* authorized a court to issue "a permanent or temporary injunction, or other order,"<sup>62</sup> however. Looking at this language and its legislative history, the Court concluded that Congress intended to authorize the district court to grant all equitable remedies. Thus the holding can be limited to the statute in question, and the Court's broader pronouncement is clearly dictum.<sup>63</sup>

In the antitrust field the federal courts have often granted ancillary relief. In *Schine Chain Theatres, Inc. v. United States*,<sup>64</sup> the Supreme Court approved a divestiture order under section 4 of the Sherman Act, which authorizes the district courts "to prevent and restrain" violations of the Act and permits the government to request that a violation "be enjoined or otherwise prohibited."<sup>65</sup> Like the statutory language "or other order" in *Porter*,<sup>66</sup> the language "or otherwise prohibited" in the Sherman Act indicates Congress envisioned equitable remedies beyond a simple injunction. Furthermore, the evils of illegal mergers which the Sherman Act is supposed to remedy, principally reduced competition,<sup>67</sup> continue after consummation of the merger; thus, one may view the continuing combina-

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61. *Id.* at 398. The Court affirmed an order requiring a landlord to refund rents collected in excess of war time rent controls. *Accord* *Weinberger v. Romero-Barcelo*, 102 S. Ct. 1798 (1982) (dictum that the court may decline to enjoin violation of federal statute).

62. Emergency Price Control Act of 1942, § 205(e), 50 U.S.C. app. § 925(a) (1976). Moreover, the legislative history clearly supported the holding by stating: "Such courts are given jurisdiction to issue whatever order to enforce compliance is proper under the circumstances of each particular case." 328 U.S. at 401 (quoting S. REP. NO. 931, 77th Cong., 2d Sess. 10 (1942)). *Cf.* *United States v. Parkinson*, 240 F.2d 918, 922 (9th Cir. 1956) (denying restitution where statute did not contain such language).

63. Similarly, in *United States v. Moore*, 340 U.S. 616, 619-20 (1951), the relevant statute permitted the court to issue an injunction "or other order." The Court upheld an order that a landlord refund rents charged in excess of war time rent controls even though no injunction was appropriate because the rental area had been decontrolled after the violations but before suit was brought.

64. 334 U.S. 110, 128-29 (1948). The Court affirmed an injunction and divestiture order against defendants found to have violated sections 1 and 2 of the Sherman Act.

65. 15 U.S.C. § 4 (1976).

66. See *supra* notes 60-63 and accompanying text.

67. L. SULLIVAN, HANDBOOK OF THE LAW OF ANTITRUST 14 (1977) ("The purpose of the antitrust laws is to promote competition and to inhibit monopoly and restraints upon freedom of trade . . .").

tion of two illegally merged firms as a continuing violation of the Sherman Act. Divestiture, then, only prevents a continuing violation of the Act.<sup>68</sup> Divestiture is intended not to impose on defendants any demand not already imposed by law, but only to deprive them of the fruit of their illegal behavior. "It is . . . designed . . . to undo what could have been prevented had the defendants not outdistanced the government in their unlawful project."<sup>69</sup> In short, divestiture merely discontinues an illegal arrangement and restores the status quo ante. One can similarly explain most other ancillary remedies under the antitrust laws<sup>70</sup> and the FTC's remedy of corrective advertising.<sup>71</sup>

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68. The Supreme Court has stated, "Dissolution of the combination will be ordered where the creation of the combination is itself the violation." *United States v. Crescent Amusement Co.*, 323 U.S. 173, 189-90 (1944). The divestiture decree required certain persons to resign from offices with corporations affiliated with the defendant exhibitors and enjoined them from occupying such offices. Interlocking managements were part of the combination which was "itself the violation," however. Thus, unlike the restructuring of corporate boards in securities cases, this relief imposed no burden not already required by law.

69. *Schine Chain Theatres, Inc. v. United States*, 334 U.S. 110, 128 (1948). *Accord* *United States v. Paramount Pictures, Inc.*, 334 U.S. 131, 171 (1948) (in remanding for reconsideration of divestiture, the Court said the district court's "function includes undoing what the conspiracy achieved"). As early as 1911, in *Standard Oil Co. v. United States*, 221 U.S. 1, 78 (1911), the Court stated that relief under the antitrust laws should simply "dissolve the combination . . . which the possession of the power unlawfully obtained has brought and will continue to bring about." The Court in *Standard Oil* overturned parts of the lower court's decree that went beyond this principle. *Id.* at 80-81. *Accord* *Ford Motor Co. v. United States*, 405 U.S. 562, 573 (1972) ("Divestiture is a start toward restoring the pre-acquisition situation.").

70. The distribution of technology was ordered in *United States v. National Lead Co.*, 332 U.S. 319, 352-58 (1947), to deprive the defendant of monopoly power acquired in violation of the Sherman Act by the pooling of patents and the allocation of markets.

71. Corrective advertising is designed, as the name implies, to deny offenders the benefits of past illegality by requiring them to correct prior deceptive advertising. Some lower court opinions approving corrective advertising have employed very broad language. *See, e.g.,* *Warner-Lambert Co. v. FTC*, 562 F.2d 749, 757 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 950 (1978) ("the Commission has the power to shape remedies which go beyond the simple cease and desist order"). *See also* *Jacob Siegel Co. v. FTC*, 327 U.S. 608, 612-13 (1946) ("the courts will not interfere [with the Commission's selection of a remedy] except where the remedy selected has no reasonable relation to the unlawful practices found to exist.") In *Jacob Siegel*, however, the question was whether the Commission properly ordered excision of a trade name it deemed inherently deceptive. Assuming the trade name was deceptive, forbidding its continued use would be simply to forbid a continued violation of the law.

Commentators have recognized that depriving defendants of the fruits of past illegality is the purpose of corrective advertising. *See, e.g.,* Pitofsky, *Beyond Nader: Consumer Protection and the Regulation of Advertising*, 90 HARV. L. REV. 661, 696 (1977) ("the Commission must have the authority to deprive il-



In *Mitchell v. DeMario Jewelry, Inc.*,<sup>72</sup> the Supreme Court approved reimbursement of wages lost by an employee wrongfully discharged, even though the relevant statute denied the courts jurisdiction to order payment to employees of "unpaid minimum wages or unpaid overtime compensation." While the statute in *Mitchell* authorized the Secretary of Labor only to seek an injunction,<sup>73</sup> and thus the case cannot be distinguished on the same grounds as *Porter* and *Schine*,<sup>74</sup> the ancillary relief granted there only required compensation for past violations of the law and imposed no burden on the defendant's future behavior. Thus, even if *Mitchell* supports ancillary relief to rectify past violations of the law, it hardly supports remedies affecting future behavior.

A few lower court cases have held that certain administrative agencies were not authorized by statute to obtain certain remedies.<sup>75</sup> Furthermore, courts have limited the powers of administrative agencies in ways significant to ancillary relief. An agency may not issue an order which is a "patent attempt to achieve ends other than those which can fairly be said to effectuate the policies of" the enabling statute.<sup>76</sup> While these cases

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legal advertisers of the unlawful fruits of their violations in order to reestablish the market situation as it existed prior to the wrongdoing").

72. 361 U.S. 288 (1960).

73. Section 17 of the Fair Labor Standards Act authorized courts only "to restrain violations" of the Act. 361 U.S. at 289.

74. See *supra* notes 62, 65 and accompanying text.

75. In *United States v. Parkinson*, 240 F.2d 918 (9th Cir. 1956), the court held that the FDA was not entitled to restitution after a violation of the Federal Drug and Cosmetic Act. Several cases have held that a court may not order a product recall as an ancillary remedy under the same Act. See *United States v. Superpharm Corp.*, 530 F. Supp. 408, 410-11 (E.D.N.Y. 1981); *United States v. X-Otag Plus Tablets*, 441 F. Supp. 105, 115 (D. Colo. 1977); *United States v. C.E.B. Prods., Inc.*, 380 F. Supp. 664, 672 (N.D. Ill. 1974). Cf. *National Confectioners Ass'n v. Califano*, 569 F.2d 690, 694 (D.C. Cir. 1978) (dictum that the FDA does not have authority to mandate recalls). But see *United States v. K-N Enterprises, Inc.*, 461 F. Supp. 988 (N.D. Ill. 1978) (factors allowing preliminary injunction pendente lite to issue requiring recall).

In a few administrative law cases the Supreme Court has ruled that federal statutes barred certain ancillary equitable remedies. All these cases have involved suits *against* administrative agencies and might be distinguished from other ancillary relief cases on that ground, though the Court has sometimes discussed these cases as if they were indistinguishable. See *Renegotiation Bd. v. Bannercrest Clothing Co.*, 415 U.S. 1, 18-19 (1974) (discussing *Porter Co. v. NLRB*, 397 U.S. 99 (1970)). But these cases differ from the ancillary relief cases in other ways. See *Renegotiation Bd.*, 415 U.S. at 20 (holding respondent had to exhaust administrative remedies before challenging Board's action in court); *Switchmen's Union v. National Mediation Bd.*, 320 U.S. 297, 301-02 (1943) (petition to the Board held to be the exclusive remedy, precluding judicial relief).

76. *Virginia Elec. & Power Co. v. NLRB*, 319 U.S. 533, 540 (1943) (dictum; Court upheld an NLRB order because there was no showing of any such at-

do not involve ancillary relief of the kind obtained by the SEC, they do delimit the permissible scope of administrative action and at least suggest that ancillary remedies, if permitted at all, must be carefully designed so as not to exceed the purposes of the relevant statute.

The imposition of restitution and other conditions to probation in a criminal sentence is superficially similar to ancillary equitable remedies. This use of probation provides little support for ancillary equitable relief, however, because of the procedural protections available to criminal defendants and because the federal probation statute expressly authorizes imposition of "such terms and conditions as the court deems best."<sup>77</sup>

In sum, Supreme Court cases approving ancillary relief in

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tempt in the case). Thus, the NLRB may not order an employer to grant a union a particular concession in a collective bargaining agreement, *Porter Co. v. NLRB*, 397 U.S. 99, 106-07 (1970); *NLRB v. American Nat'l Ins. Co.*, 343 U.S. 395, 404 (1952), and the FPC may not prohibit employment discrimination by its regulatees, *NAACP v. FPC*, 425 U.S. 662, 669-71 (1976). The Court denied that the statutory criterion of the public interest is "a broad license to promote the general public welfare. Rather, the words take meaning from the purposes of the regulatory legislation." *Id.* at 669. Arguably, an administrative agency cannot obtain by judicial relief that which it cannot demand by rule or order.

77. 18 U.S.C. § 3651 (1976). The statute expressly permits a court to grant probation "upon such terms and conditions as the court deems best," including "restitution or reparation to aggrieved parties." Thus conditions to probation are not judicially implied, as are ancillary equitable remedies in securities law. For support of creative use of conditions to probation in criminal sentences against corporations, see Coffee, "No Soul to Damn: No Body to Kick": *An Unscandalized Inquiry into the Problem of Corporate Punishment*, 79 MICH. L. REV. 386, 448-57 (1981); Note, *Structural Crime and Institutional Rehabilitation: A New Approach to Corporate Sentencing*, 89 YALE L.J. 353 (1979). Among the many protections afforded criminal but not civil defendants are the necessity of the prosecution's obtaining a grand jury indictment, the right to a jury trial, the requirement that the prosecution prove its case beyond reasonable doubt, and limitations on the prosecution's ability to discover evidence from defendants. FED. R. CRIM. P. 11(f) also demands that before accepting a guilty plea the court must satisfy itself that there is a factual basis for the plea. This contrasts with the procedure in consent cases involving ancillary relief where judicial scrutiny is usually minimal. See *infra* notes 131-37 and accompanying text. These procedural protections reduce the likelihood that the court will impose a sanction on an innocent defendant.

Moreover, although the trial court's power to fashion conditions to probation is broad, it is not unlimited, and there is little or no precedent for restructuring corporate managements as a condition to probation. See *Higdon v. United States*, 627 F.2d 893, 897 (9th Cir. 1980) (conditions to probation must be narrowly drawn to achieve rehabilitation and protection of the public without unnecessarily restricting lawful activities); *United States v. Pastore*, 537 F.2d 675, 683 (2d Cir. 1976) (condition that defendant resign from the bar held invalid in sentence of probation); *United States v. Atlantic Richfield Co.*, 465 F.2d 58, 61 (7th Cir. 1972) (order requiring corporation to institute pollution control program was unreasonable and exceeded district court's authority).

administrative law are limited to a few holdings under specific statutes and some broader dicta. Many cases strongly suggest, even if they do not clearly hold, that ancillary relief may be granted only to terminate a continuing violation of law or to deprive a wrongdoer of the fruits of past transgressions. The precedents do not establish that an administrative agency is entitled to whatever relief it or the court thinks beneficial. At the least, the law of ancillary relief is sufficiently amorphous to leave the Supreme Court much leeway when it tackles the issue. Moreover, even the limited authority for ancillary relief may be undermined by recent Supreme Court decisions concerning statutory interpretation, federal common law, and implied statutory remedies.

#### B. FEDERAL EQUITY, STATUTORY INTERPRETATION, AND FEDERAL COMMON LAW

Perhaps the principal justification for ancillary relief in administrative law has been the equitable power of federal courts to fashion remedies to enforce federal statutes.<sup>78</sup> Courts and commentators have often trumpeted the powers of equity: "The power of equity knows no limit . . . , there is no limit to the various forms and kinds of specific remedy which [the chancellor] may grant."<sup>79</sup> The Supreme Court has also stated

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78. See *Deckert v. Independence Shares Corp.*, 311 U.S. 282, 288 (1940); *Handler v. SEC*, 610 F.2d 656, 659 (9th Cir. 1979); *SEC v. Commonwealth Chem. Secs. Corp.*, 574 F.2d 90 (2d Cir. 1978); *SEC v. Investors Sec. Corp.*, 560 F.2d 561, 567 (3d Cir. 1977); *SEC v. Lincoln Thrift Ass'n*, 557 F.2d 1274, 1276 (9th Cir. 1977); *Chris-Craft Indus., Inc. v. Piper Aircraft Corp.*, 480 F.2d 341, 379 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973); *SEC v. Radio Hill Mines Co.*, 479 F.2d 4, 6 (2d Cir. 1973); *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1100 (2d Cir. 1972); *SEC v. Texas Gulf Sulphur Co.*, 446 F.2d 1301, 1308 (2d Cir. 1971), *cert. denied*, 404 U.S. 1005 (1972); *SEC v. Bartlett*, 422 F.2d 475, 478 (8th Cir. 1970); *SEC v. S & P Nat'l Corp.*, 360 F.2d 741, 747 (2d Cir. 1966); *Lankenau v. Coggeshall & Hicks*, 350 F.2d 61, 63 (2d Cir. 1965); *Los Angeles Trust Deed & Mortgage Exch. v. SEC*, 285 F.2d 162, 181-82 (9th Cir. 1960), *cert. denied*, 366 U.S. 919 (1961); *SEC v. Western Geothermal & Power Corp.*, [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,920, at 95,860 (D. Ariz. 1979); *SEC v. Falstaff Brewing Corp.*, [1977-78 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,117, at 92,020 (D.D.C. 1977); *SEC v. Weisberger*, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,108, at 97,943 (S.D.N.Y. 1975); *SEC v. American Inst. Counselors, Inc.*, [1975-76 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,388, at 98,962 (D.D.C. 1975); *SEC v. General Refractories Co.*, 400 F. Supp. 1248, 1254 (D.D.C. 1975); *SEC v. R.J. Allen & Assocs., Inc.*, 386 F. Supp. 866, 875 (S.D. Fla. 1974); *SEC v. Shapiro*, 349 F. Supp. 46, 55 (S.D.N.Y. 1972), *aff'd*, 494 F.2d 1301 (2d Cir. 1974); *SEC v. Wong*, 252 F. Supp. 608, 613 (D.P.R. 1966); *SEC v. Gulf Intercont. Fin. Corp.*, 223 F. Supp. 987, 996 (S.D. Fla. 1963); *SEC v. H.S. Simmons & Co.*, 190 F. Supp. 432, 432-33 (S.D.N.Y. 1961); *Kardon v. National Gypsum Co.*, 73 F. Supp. 798, 802-03 (E.D. Pa. 1947).

79. 1 J. POMEROY, *supra* note 5, § 109.

that in fashioning remedies, courts of equity have flexibility to afford complete relief.<sup>80</sup> Although the powers of equity are broad, they are not boundless. Equity is regulated by the rules of pleading and procedure.<sup>81</sup> In fashioning equitable remedies, the federal courts must adhere to the traditional practices of equity: "When Congress leaves to the federal courts the formulation of remedial details, it can hardly expect them to break with historic principles of equity in the enforcement of federally-created equitable rights."<sup>82</sup> Rather, the Court has insisted on following "the requirements of equity practice with a background of several hundred years of history."<sup>83</sup> It has referred to using traditional or familiar remedies<sup>84</sup> and has refused to approve a remedy for which there was no precedent "in the long history of equity jurisprudence."<sup>85</sup> The Court has also im-

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80. *Swann v. Charlotte-Mecklenburg Board of Ed.*, 402 U.S. 1, 15 (1971). See also *Weinberger v. Romero-Barcelo*, 102 S. Ct. 1798, 1803 (1982); *Hecht Co. v. Bowles*, 321 U.S. 321, 329-30 (1944).

81. 1 J. POMEROY, *supra* note 5, § 115.

82. *Holmberg v. Armbrrecht*, 327 U.S. 392, 395 (1946). See also *Albemarle Paper Co. v. Moody*, 422 U.S. 405, 416, 417 (1975) (the chancellor's "judgment is to be guided by sound legal principles" and not vary "like the chancellor's foot"); *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 60-61 (1975) (referring to "traditional prerequisites" to equitable relief); *Whitcomb v. Chavis*, 403 U.S. 124, 160-61 (1971) (lower court overstepped equity power and usurped legislative power by fixing voting districts); *Board of Commissioners v. United States*, 308 U.S. 343, 349-50, 351-52 (1939) (considerations of fairness precluded payment of interest for use of money); P. BATOR, P. MISHKIN, D. SHAPIRO & H. WECHSLER, *HART & WECHSLER'S THE FEDERAL COURTS AND THE FEDERAL SYSTEM* 1311 (2d ed. 1973) [hereinafter *HART & WECHSLER*] ("a statutory jurisdiction to grant injunctions is to be administered in the light of general equitable principles").

83. *Hecht Co. v. Bowles*, 321 U.S. 321, 329 (1944). *Accord* *Weinberger v. Romero-Barcelo*, 102 S. Ct. 1798, 1803 (1982) ("we do not lightly assume that Congress has intended to depart from established principles").

84. See *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 102 S. Ct. 1825, 1838 (1982) (quoting *Frankfurter, J.*, dissenting in *Montana-Dakota Util. Co. v. Northwestern Pub. Serv. Co.*, 341 U.S. 246, 261 (1951)) ("Courts . . . do not require explicit statutory authorization for familiar remedies to enforce statutory obligation . . . . [O]ur function is to decide what remedies are appropriate in the light of the statutory language and purpose and of the traditional modes by which courts compel performance."); *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 61-62 (1975) ("traditional remedies"); *Bivens v. Six Unknown Named Agents*, 403 U.S. 388, 402-03 n.4 (1971) (*Harlan, J.*, concurring) (referring to "a choice among *traditionally available* judicial remedies") (emphasis in original).

85. In *De Beers Consol. Mines, Ltd. v. United States*, 325 U.S. 212, 223 (1945), an antitrust case, the Supreme Court overturned the district court's grant of an interlocutory injunction which amounted to a sequestration of assets. The Court concluded that the antitrust laws did not authorize such relief and then considered "the general principles which govern the granting of equitable relief." *Id.* at 218-19. The Court paid little attention to the lower court's conclusion on the facts that such relief was desirable. Finding no precedent for such relief, the Court rejected it as "not authorized . . . by statute or by the

posed many specific restrictions on federal equity, particularly on when a court may grant an injunction<sup>86</sup> or appoint a receiver.<sup>87</sup> In addition, equitable relief must be appropriate<sup>88</sup> and, in determining this propriety, courts may have to weigh factors other than the plaintiff's need for complete relief. In particular, relief must effectuate the purposes of the law under which relief is afforded.<sup>89</sup>

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usages of equity . . . ." *Id.* at 223. See also *United States v. Paramount Pictures*, 334 U.S. 131, 176 (1948) (district court has no power to require parties to submit to arbitration); *Central Ky. Natural Gas Co. v. Railroad Comm'n*, 290 U.S. 264, 271-73 (1933) (there are limits on conditions court can attach to an injunction; injunction may not be conditioned so that court in effect sets utility rates).

86. For the issuance of an injunction the Court has required: (1) "a definite factual showing of illegality," *Standard Oil Co. v. United States*, 283 U.S. 163, 179 (1931); *accord* *Appalachian Coals, Inc. v. United States*, 288 U.S. 344, 377 (1933); *Chicago Board of Trade v. United States*, 246 U.S. 231, 238 (1918); (2) a threat of irreparable harm, at least in certain cases, *Weinberger v. Romero-Barcelo*, 102 S. Ct. 1798, 1803 (1982); *Kleppe v. Sierra Club* 427 U.S. 390, 407-08 (1976) (concerning the National Environmental Policy Act); *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 61 (1975) (concerning § 13(d) of the Exchange Act); (3) a reasonable likelihood that future violations will occur if the injunction does not issue, *Aaron v. SEC*, 446 U.S. 680, 701 (1980); *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 59 (1975); and (4) proof of the inadequacies of remedies at law, *O'Shea v. Littleton*, 414 U.S. 488, 502 (1974). Any injunction must relate closely to the defendant's past or threatened infractions. *May Stores Co. v. NLRB*, 326 U.S. 376, 392 (1945); *NLRB v. Express Publ. Co.*, 312 U.S. 426, 437 (1941). See also *FTC v. Mandel Bros.*, 359 U.S. 385, 392 (1959) (order enforced because activity enjoined was closely related to the illegal conduct); *De Beers Consol. Mines, Ltd. v. United States*, 325 U.S. 212, 217, 222 (1945) (injunction dissolved where it dealt with "a matter lying wholly outside the issues in the case," and was "unrelated to any supposed violations of the Anti-Trust Laws"). The Court has stressed the need to limit the remedy to the violation in many recent cases. See, e.g., *Dayton Bd. of Educ. v. Brinkman*, 433 U.S. 406, 419 (1977) (remand due to disparity between violations and "sweeping remedy"); *Milliken v. Bradley (Milliken II)*, 433 U.S. 267, 280 (1977); *Milliken v. Bradley*, 418 U.S. 717, 744-45 (1974) (instance of segregation did not justify "broad metropolitan remedy"). But cf. *Porter v. Warner Holding Co.*, 328 U.S. 395, 398 (1946) ("the court may go beyond the matters immediately underlying its equitable jurisdiction"). An injunction must be designed to deter violations rather than to punish them. *Missouri-Portland Cement Co. v. H.K. Porter Co.*, 535 F.2d 388 (8th Cir. 1976); *Electronic Specialty Corp. v. International Controls Corp.*, 409 F.2d 937 (2d Cir. 1969).

87. See *infra* notes 344-65 and accompanying text.

88. *Davis v. Passman*, 442 U.S. 228, 244 (1979) (court must determine whether a damage action is "an appropriate form of relief"). See also *Bivens v. Six Unknown Named Agents*, 403 U.S. 388, 392 (1971) (federal courts will adjust their remedies to grant "necessary relief") (quoting *Bell v. Hood*, 327 U.S. 678, 684 (1946)).

89. Equitable discretion "must be exercised in light of the large objectives of the [applicable] Act." *Hecht Co. v. Bowles*, 321 U.S. 321, 331 (1944). See also *Albemarle Paper Co. v. Moody*, 422 U.S. 405, 416 (1975) (quoting *Hecht*); *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 62 (1975) (court will fashion remedies "consistent with the legislative scheme"). Thus, in *A.C. Frost & Co. v. Coeur D'Alene Mines Corp.*, 312 U.S. 38, 43 (1941), the Supreme Court reversed the in-

More important than specific dicta or holdings regarding equity, though, are the Supreme Court's new attitudes toward statutory interpretation and federal common law that will undoubtedly affect equitable remedies in a profound, but as yet undetermined way. In interpreting statutes the Court has edged away from a purposive approach, which often relied on broad inferences from general statements in statutes or legislative history, toward a more literalist approach that follows the plain meaning of a statute absent a clear statement of a contrary congressional intent in the legislative history.<sup>90</sup> Policy and equitable considerations, therefore, play a much smaller role in the current approach.<sup>91</sup>

The Court has also taken a more restrictive attitude toward federal common law—the law made by judges to decide issues committed to federal law but not covered by the Constitution or federal legislation.<sup>92</sup> In the nonconstitutional realm federal common law “shades into” statutory interpretation.<sup>93</sup> In several recent cases the Court has stressed that “federal courts, unlike their state counterparts, are courts of limited jurisdiction that have not been vested with open-ended lawmaking powers.”<sup>94</sup> The Court has grown hesitant to fashion federal common law except where Congress clearly intended it to do

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validation of a contract that violated the 1933 Act because under the facts of the case this remedy “would probably seriously hinder rather than aid the real purpose of the statute.”

90. See Note, *Intent, Clear Statement, and the Common Law: Statutory Interpretation in the Supreme Court*, 95 HARV. L. REV. 892 (1982). But see *Pennhurst State School v. Halderman*, 451 U.S. 1, 18 (1981) (court must look to “whole law, and to its object and policy”) (quoting *Philbrook v. Glodgett*, 421 U.S. 707, 713 (1975)). The “purposive” approach looked to broad legislative purpose and equitable considerations. Note, *supra*, at 893.

91. See Note, *supra* note 90, at 896-97, 901. The position taken there is somewhat overstated, however. Although some recent statements by members of the Court, usually in minority opinions, have suggested that policy and equitable considerations are irrelevant to statutory interpretation, the Court continues to weigh these factors in many majority opinions. This is not surprising, even given an approach that purportedly looks solely to congressional intent, because judges properly hesitate to assume that Congress intended to create inequity or an undesirable policy. In most opinions purporting to reject policy or equitable considerations, the author of the opinion does not reject compelling policy or equitable considerations in favor of a literal statutory reading. Instead, the writer finds such considerations conflicting and, rather than choosing between the conflicting considerations, resorts to the literal statutory language.

92. HART & WECHSLER, *supra* note 82, at 770.

93. *Id.*: “Statutory interpretation shades into judicial lawmaking on a spectrum, as specific evidence of legislative advertence to the issue at hand attenuates.” See also Note, *Implied Causes of Action: A Product of Statutory Construction or the Federal Common Law Power?*, 51 U. COLO. L. REV. 355, 393 (1980).

94. *Northwest Airlines, Inc. v. Transport Workers Union of America*, 451

so or where necessary to decide questions committed to federal law.<sup>95</sup> Thus, legislation that appears comprehensive on its face is deemed to preempt federal common law on the subject, even where Congress has not expressed any intent to preempt.<sup>96</sup> The Court is especially reluctant to fashion remedies for violations of a federal statute for which Congress has provided express remedies.<sup>97</sup> Federalism demands further hesitation to create federal common law where important state interests are at stake.<sup>98</sup>

There are several reasons for the Court's changed attitudes toward statutory interpretation and federal common law. First, the Court now believes itself incompetent to make the difficult policy decisions necessary in fashioning a broad common law or in using a purposive approach to statutory construction.<sup>99</sup> Second, the Court has become more concerned about states' rights.<sup>100</sup> Third, the Court has adopted a different vision of the

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U.S. 77, 95 (1981). *Accord* Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran, 102 S. Ct. 1825 (1982); *United States v. Standard Oil Co.*, 332 U.S. 301, 313 (1947).

95. In *Jackson Transit Auth. v. Transit Union Local 1285*, 102 S. Ct. 2202, 2210 (1982), for example, the Court held that the question whether federal law governed the enforcement of contracts mandated by federal law was to be decided by reference to congressional intent. Finding no congressional intent to federalize the law of these contracts, the Court relegated the plaintiff to state courts and state contract law. *See also* *Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 642-43 (1981) (Congress intended federal courts to create common law in applying the Sherman Act); *Northwest Airlines, Inc. v. Transport Workers Union of America*, 451 U.S. 77, 95 (1981) (federal common law is subject to congressional control).

96. Thus, in *City of Milwaukee v. Illinois*, 451 U.S. 304 (1981), the Court held that federal legislation concerning interstate water pollution preempted federal common law on the subject. The Court stated that the question of preemption of federal common law differs markedly from the question of preemption of state law. Respect for state sovereignty demands a clear, unambiguous statement by Congress to preempt state law. As to federal common law, however, the federal lawmaking power is vested in Congress, and it is assumed that, absent special circumstances, Congress, and not the courts, is to make federal law. *Id.* at 316-17. *Accord* *Middlesex County Sewerage Auth. v. National Sea Clammers Ass'n*, 453 U.S. 1, 21-22 (1981) (FWPCA preempts federal common law of water nuisance). *See also* *Northwest Airlines, Inc. v. Transport Workers Union of America*, 451 U.S. 77, 95 (1981) (federal courts have not been vested with open-ended lawmaking powers).

97. *See, e.g.*, *Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 644-46 (1981); *Northwest Airlines, Inc. v. Transport Workers Union of America*, 451 U.S. 77, 94-95 (1981).

98. *See* *United States v. Yazell*, 482 U.S. 341, 352 (1966); Note, *supra* note 93, at 375.

99. *See* Note, *supra* note 90, at 901-02. *See also* Goldstein, *A Swann Song for Remedies: Equitable Relief in the Burger Court*, 13 HARV. C.R.-C.L. L. REV. 1, 43-44 (1978) (Court has limited remedies in several recent constitutional cases because it could not acquire and use sufficient technical data, develop standards, and provide continuing supervision).

100. In one sphere of federal common law, the fashioning of constitutional

legislative process, a vision more sensitive to the compromises entailed in legislation and correspondingly more skeptical of construing complex, technical statutes by reference to a vague, poorly articulated congressional purpose.<sup>101</sup> Thus, the Court assumes that where Congress has enacted a comprehensive statute, it did not intend to leave the federal judiciary free to fashion common law in the same area.<sup>102</sup> Fourth, and most important, the Court wants to restore what it considers the appropriate constitutional balance between the legislative and judicial branches.<sup>103</sup> Underlying these attitudes is a more con-

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remedies, this growing concern has resulted in the Court's breathing new life into the doctrine of federalism. See Goldstein, *supra* note 99, at 8-26 (growing consideration of federalism in fashioning constitutional remedies). The Court is increasingly willing to declare unconstitutional federal legislation that infringes upon state interests. See *National League of Cities v. Usery*, 426 U.S. 833 (1976) (overruling *Maryland v. Wirtz*, 392 U.S. 183 (1968)). In the legislative sphere, the Court has insisted on a clear statement by Congress to sustain a statutory interpretation that would infringe upon state interests, see *Employees of Dept. of Public Health & Welfare v. Department of Public Health & Welfare*, 411 U.S. 279, 285 (1973), or to support an implied private right of action, see *infra* notes 116-22 and accompanying text. Especially in the securities field the Court has hesitated to interpret federal law so as to overlap or to interfere with state law. See *infra* notes 226-40 and accompanying text.

101. See *Diamond v. Chakrabarty*, 447 U.S. 303, 317 (1980) (legislation "involves the balancing of competing values and interests"). *Accord Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 647 (1981). See also *Mohasco Corp. v. Silver*, 447 U.S. 807, 818-19 (1980); ("The present language was clearly the result of a compromise."); Note, *supra* note 90, at 900-02 ("In the pluralistic society, the only shared values are those that emerge . . . from the legislative battleground."). Although the broad congressional purpose may be apparent, it may be too vague to determine the consistency of a particular interpretation with the congressional intent, e.g., a right to contribution among joint antitrust violators, *Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630 (1981); or a particular construction of a statute of limitations, *Mohasco Corp. v. Silver*, 447 U.S. 807 (1980).

102. See *Middlesex County Sewerage Auth. v. National Sea Clammers Ass'n.*, 453 U.S. 1, 14-15, 20 (1981); *Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 645 (1981); *Northwest Airlines, Inc. v. Transport Workers Union of America*, 451 U.S. 77, 97 (1981). The Court has cited the increasing complexity of federal legislation as justification for refusing to supplement such legislation with federal common law or to stray far from the statutory language in construing such legislation. See *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 102 S. Ct. 1825, 1838-39 (1982).

103. "[W]e consistently have emphasized that federal lawmaking power is vested in the legislative, not the judicial, branch of government; . . ." *Northwest Airlines, Inc. v. Transport Workers Union of America*, 451 U.S. 77, 95 (1981). The Court has not made clear to what extent its new attitudes are constitutionally mandated or are discretionary judicial policies. On occasion the Court has cited the separation of powers principle to justify its holdings. See, e.g., *City of Milwaukee v. Illinois*, 451 U.S. 304, 315 (1981). On other occasions the Court has denied that its decisions were constitutionally mandated. See, e.g., *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 102 S. Ct. 1825, 1837-39 (1982). See *infra* note 146. The Court's attitudes reflect dissatisfaction with the activist, "imperial" judiciary, a dissatisfaction undoubtedly due substan-



servative political philosophy that includes hostility to government regulation of business.<sup>104</sup>

The Court's current attitudes create a new context within which federal equity must be viewed. A federal court's equitable remedial powers differ considerably in constitutional and nonconstitutional cases. Even though the Burger Court has also narrowed constitutional remedies, the courts' remedial power is much broader in constitutional cases, where the power of Congress is not absolute, or even preeminent, than it is elsewhere.<sup>105</sup> In nonconstitutional cases the limits of statutory interpretation and federal common law and the Court's new attitudes in these areas constrict a federal court's equitable powers. Of course, Congress may grant certain equitable powers to the federal courts under a statute, but the Court will not automatically assume or readily infer such a grant. Neither will the Court fashion equitable remedies under the federal common law as readily as it has before.<sup>106</sup>

Since the Supreme Court has not recently discussed ancillary relief in administrative law, the relevance of these trends in statutory interpretation and federal common law cannot yet

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tially to politically conservative dissatisfaction with the liberal agenda advanced by judicial activists. *See infra* note 104.

104. The Supreme Court justices appointed by Presidents Nixon, Ford, and Reagan were intended to create a more conservative Court. *See Note, supra* note 90, at 900 n.66, 910-11, and authorities cited therein. The Court's more literal approach to statutory construction has produced some liberal decisions, however. *See, e.g.,* North Haven Bd. of Educ. v. Bell, 102 S. Ct. 1912 (1982) (literal language of antidiscrimination provisions of Education Amendments of 1972 applies to employees as well as to students).

105. *See Davis v. Passman*, 442 U.S. 228, 241 (1979) ("the question of who may enforce a *statutory* right is fundamentally different from the question of who may enforce a right that is protected by the Constitution," because the judiciary is "the primary means through which [constitutional] rights may be enforced") (emphasis in original). *See also Bivens v. Six Unknown Named Agents*, 403 U.S. 388, 396-97 (1971) (distinguishing *Wheeldin v. Wheeler*, 373 U.S. 647 (1963), as involving "merely" a statutory violation). Thus, the equitable jurisdiction of American courts is fixed "by the extent and limitations of statutory authority." 1 J. POMEROY, *supra* note 5, § 282. The distinction between statutory and constitutional cases has been clearest in the Court's treatment of implied private damage actions. *See infra* note 144.

Even in constitutional cases, the Burger Court has restricted the scope of remedies. In particular, the Court has insisted that remedies be tailored to the scope of the constitutional violation. *See Goldstein, supra* note 99, at 61-62. *See also supra* note 92.

106. *See City of Milwaukee v. Illinois*, 451 U.S. 304, 317 (1981), where the Court denied that Congress had "left the formulation of appropriate federal standards to the courts through application of often vague and indeterminate nuisance concepts and maxims of equity jurisprudence" and refused to fashion federal common law in an area where Congress had established "a comprehensive regulatory program supervised by an expert administrative agency."

be determined. Many recent decisions, however, have dealt with implied remedies under federal statutes, and these cases provide some framework for analyzing the propriety of ancillary relief.

### C. IMPLIED STATUTORY REMEDIES

Courts and commentators approving ancillary relief in securities law have often relied on cases implying the existence of private rights of action.<sup>107</sup> They have reasoned that if a court, under its equitable powers, can imply the remedy of a private damage action, it should also be able to imply equitable remedies ancillary to an injunction. Moreover, courts finding implied rights of action have often used reasoning very like that used to approve ancillary relief.<sup>108</sup> It is therefore appropriate to review the Supreme Court's recent pronouncements concerning implied private rights of action and other implied remedies.

The leading authority for broad implication of private rights of action and other remedies is *J.I. Case Co. v. Borak*,<sup>109</sup> which upheld a private action for rescission or damages under section 14(a) of the Exchange Act. As in *Deckert*,<sup>110</sup> the Court relied on the statute granting the federal district courts jurisdiction over suits "to enforce any liability or duty created" by

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107. See *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082 (2d Cir. 1972); *SEC v. Texas Gulf Sulphur Co.*, 446 F.2d 1301, 1307-08 (2d Cir. 1971), *cert. denied*, 404 U.S. 1005 (1972); *SEC v. Western Geothermal & Power Corp.*, [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,920 (D. Ariz. 1979); *SEC v. Penn Central Co.*, 450 F. Supp. 908, 916 (E.D. Pa. 1978); *SEC v. R.J. Allen & Assocs., Inc.*, 386 F. Supp. 866 (S.D. Fla. 1974).

108. See *Kardon v. National Gypsum Co.*, 73 F. Supp. 798 (E.D. Pa. 1947), the first case to imply a private civil damage action under rule 10b-5. The court relied in large part on "well known and well established equitable principles." *Id.* at 802-03. See also *infra* text accompanying notes 110-13.

109. 377 U.S. 426 (1964). Prior to *Borak* the Supreme Court had decided several implied private action cases, but had never enunciated a clear, consistent doctrine to cover such cases. See *Hazen, Implied Private Remedies under Federal Statutes: Neither a Death Knell Nor a Moratorium—Civil Rights, Securities Regulation, and Beyond*, 33 VAND. L. REV. 1333, 1346-52 (1980).

See also *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375 (1970). In *Mills* the Court reaffirmed the broad discretion of district courts to fashion relief for violations of the proxy rules and approved awarding attorneys' fees to plaintiffs in securities law cases where they have conferred a benefit on a class. On the latter point the Court relied on "the original authority of the chancellor to do equity." 396 U.S. at 393 (quoting *Sprague v. Ticonic Bank*, 307 U.S. 161, 166 (1939)). The Court has recently limited the power of federal courts to award attorneys' fees to a prevailing party. See *infra* notes 127-28 and accompanying text.

110. See *supra* note 49 and accompanying text.

the Act.<sup>111</sup> Treating implication as a matter of federal common law<sup>112</sup> rather than statutory construction, the *Borak* Court stated that the federal courts should "be alert to provide such remedies as are necessary to make effective the congressional purpose."<sup>113</sup> The Court cited the administrative law cases upholding ancillary relief.<sup>114</sup>

In the 1970's, beginning with *Cort v. Ash*,<sup>115</sup> the Court began to change its position on implied private actions, and in two securities cases decided in 1979 the Court clarified its new position. In *Touche Ross & Co. v. Redington*,<sup>116</sup> the Court stated that "[t]he question of the existence of a statutory cause of action, is, of course, one of statutory construction . . . . [O]ur task is limited solely to determining whether Congress intended to create the private right of action asserted . . . ."<sup>117</sup>

111. 377 U.S. at 433-34. The Court also looked to the purpose of section 14(a) to protect investors and the importance of private enforcement as "a necessary supplement to Commission action." *Id.* at 432-33. Although the Court did not mention the equitable powers of federal courts, it cited several cases relying on those powers. *Id.* at 433-34.

112. See Frankel, *Implied Rights of Action*, 67 VA. L. REV. 553, 557-58 (1981).

113. 377 U.S. at 433.

114. *Id.* at 434. For a description and discussion of these cases, see *supra* notes 59-77 and accompanying text.

115. *Cort v. Ash*, 422 U.S. 66 (1975), listed four factors relevant to implication:

First, is the plaintiff 'one of the class for whose *especial* benefit the statute was enacted' . . . —that is, does the statute create a federal right in favor of the plaintiff? Second, is there any indication of legislative intent, explicit or implicit, either to create such a remedy or to deny one? . . . Third, is it consistent with the underlying purposes of the legislative scheme to imply such a remedy for the plaintiff? . . . And finally, is the cause of action one traditionally relegated to state law, in an area basically the concern of the States, so that it would be inappropriate to infer a cause of action based solely on federal law?

*Id.* at 78.

116. 442 U.S. 560 (1979).

117. *Id.* at 568 (denying an implied damage action under section 17(a) of the 1934 Act). Similarly, in *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 16 (1979), the Court stated that "The question whether a statute creates a cause of action, either expressly or by implication, is basically a matter of statutory construction . . . . [W]hat must ultimately be determined is whether Congress intended to create the private remedy asserted." See also *California v. Sierra Club*, 451 U.S. 287, 297 (1981) (no private cause of action under § 10 of the Rivers and Harbors Appropriation Act of 1899 because general ban did not indicate congressional intent to benefit a particular class of persons).

The third and fourth *Cort* factors—the consistency of the implied remedy with the underlying legislative scheme and with state law—cannot tip the balance in favor of implying a remedy if the first two factors weigh strongly against implication: "[T]he Court did not decide that each of these factors is entitled to equal weight. The central inquiry remains whether Congress intended to create, either expressly or by implication, a private cause of action." *Touche Ross & Co. v. Redington*, 442 U.S. at 575. *Accord* *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 102 S. Ct. 1825 (1982); *Middlesex County Sewer-*

Silence in the legislative history tends to militate against implication of a remedy: "[I]mplying a private right of action on the basis of congressional silence is a hazardous enterprise, at best."<sup>118</sup> The existence of express remedies also tends to militate against the implication of other remedies. "Where a statute expressly provides a particular remedy or remedies, a court must be chary of reading others into it."<sup>119</sup> If refusal to infer a private action "sanctions injustice," Congress must remedy the problem, for the courts "are not at liberty to legislate."<sup>120</sup> The Court rejected the reasoning in *Borak* that section 27 of the Exchange Act justifies the implication of remedies.

Section 27 grants jurisdiction to the federal courts and provides for venue and service of process. It creates no cause of action of its own force and effect; it imposes no liabilities. The source of plaintiffs' rights must be found, if at all, in the substantive provisions of the 1934 Act

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age Auth. v. National Sea Clammers Ass'n, 453 U.S. 1, 13 (1981); *California v. Sierra Club*, 451 U.S. 287, 298 (1981).

118. *Touche Ross & Co. v. Redington*, 442 U.S. at 571. The Court said further that

[w]here . . . the plain language of the provision weighs against implication of a private remedy, the fact that there is no suggestion whatsoever in the legislative history that § 17(a) may give rise to suits for damages reinforces our decision not to find such a right of action implicit within the section.

*Id.* "[L]egislative silence is not always the result of a lack of prescience; it may instead be token permission, or perhaps, considered abstention from regulation . . . . Accordingly, caution must temper judicial creativity in the face of legislative or regulatory silence." *Ford Motor Credit Co. v. Milhollin*, 444 U.S. 555, 565 (1980). See also *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 102 S. Ct. 1815 (1982); *California v. Sierra Club*, 451 U.S. 287, 296 (1981); *Cort v. Ash*, 422 U.S. 66, 82-84 (1975). Cf. *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 18 (1979) ("while the absence of anything in the legislative history that indicates an intention to confer any private right of action is hardly helpful to the respondent, it does not automatically undermine his position"); *Cannon v. University of Chicago*, 441 U.S. 677, 694-703 (1971) (Court found implied private right of action under Title IX of the Education Amendments of 1972 largely because of clear evidence in the legislative history that Congress intended to create such a remedy).

119. *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 19 (1979). Accord *Middlesex County Sewerage Auth. v. National Sea Clammers Ass'n*, 453 U.S. 1, 14 (1981). The Court in *Transamerica* noted that Congress had provided several means for enforcing compliance and found it "highly unlikely that 'Congress absentmindedly forgot to mention an intended private action.'" 444 U.S. at 20. To make this point the Court has revived the maxim *expressio unius est exclusio alterius*—the expression of one thing is the exclusion of others. *National R.R. Passenger Corp. v. National Ass'n of R.R. Passengers*, 414 U.S. 453, 458 (1974). In *Transamerica* the Court held that the express provision for injunctions tended to negate any implied private damage action. 444 U.S. at 20. That the express remedy also negates ancillary relief would seem to follow a fortiori.

120. *Touche Ross & Co. v. Redington*, 442 U.S. 560, 579 (1979). See also *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 23-24 (1979) (citing *Touche Ross*); *infra* note 286.

...<sup>121</sup>

Finally, the Court limited *Borak* to its special facts.<sup>122</sup>

While denying a private damage action, *Transamerica Mortgage Advisors, Inc. v. Lewis*,<sup>123</sup> upheld a private action for the equitable remedies of rescission or restitution. The Court relied solely on the statutory language, however, and approved only the equitable remedies expressly indicated.<sup>124</sup> In several actions for injunctions the Court has applied the same analysis as in the private damage suits without noting any distinction based on the nature of the relief sought.<sup>125</sup> Thus implication of

121. *Touche Ross & Co. v. Redington*, 442 U.S. at 577. Section 27 and its counterpart in the 1933 Act, section 22(a), have been called the primary authority for ancillary relief. Gruenbaum & Steinberg, *Section 29(b) of the Securities Exchange Act of 1934: A Viable Remedy Awakened*, 48 GEO. WASH. L. REV. 1, 52 (1979). Even the brief for Touche Ross had not taken the position adopted by the Court. Reply Brief for Petitioner Touche Ross & Co. at 19-20, *Touche Ross & Co. v. Redington*, 442 U.S. 560 (1977). Indeed, in *Transamerica*, because the relevant legislative history showed that Congress had deleted reference to "actions at law" from the jurisdictional provision, leaving only actions "in equity," the Court found that the section affirmatively supported the conclusion that Congress did not intend any private damage actions. *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 22 (1979). See *Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 640-41 (1981) ("The vesting of jurisdiction in the federal courts does not in and of itself give rise to authority to formulate federal common law . . ."); HART & WECHSLER, *supra* note 82, at 786 ("in the legal system generally a jurisdictional grant does not in and of itself necessarily—or even ordinarily—imply a power to make substantive rules of decision"). See also *United States v. Testan*, 424 U.S. 393, 398 (1976) (grant of jurisdiction to Court of Claims "does not create any substantive right"). But see Greene, *Judicial Implication of Remedies for Federal Statutory Violations: The Separation of Powers Concerns*, 53 TEMP. L.Q. 469 (1980) (courts have power to determine whether to allow remedy to statutory violation).

122. To the extent that our analysis in today's decision differs from that of the Court in *Borak*, it suffices to say that in a series of cases since *Borak* we have adhered to a stricter standard for the implication of private causes of action, and we follow that stricter standard today.

*Touche Ross & Co. v. Redington*, 442 U.S. at 578. Justice Rehnquist, who wrote the majority opinion, expressed the same idea even more strongly dissenting in *Carlson v. Green*, 446 U.S. 14, 39-40 n.5 (1980), in which he stated that after *Touche Ross* and *Transamerica* "it is clear that there is nothing left of the rationale of *Borak*."

123. 444 U.S. 11 (1979).

124. Section 215 declared void contracts made in violation of the Investment Advisers Act. The Court concluded that Congress "intended that the customary legal incidents of voidness would follow, including the availability of a suit for rescission . . . and for restitution." *Id.* at 19. The Court expressly ruled out other equitable relief, *id.* at 24, and carefully limited the scope of the right to restitution, *id.* at 24 n.14. See generally Gruenbaum & Steinberg, *supra* note 121 (similar language under § 29(b) of Exchange Act).

125. *Middlesex County Sewerage Auth. v. Nat'l Sea Clammers Ass'n*, 453 U.S. 1 (1981); *California v. Sierra Club*, 451 U.S. 287 (1981); *Securities Investor Protection Corp. v. Barbour*, 421 U.S. 412 (1975); *National R.R. Passenger Corp. v. Nat'l Ass'n of R.R. Passengers*, 414 U.S. 453 (1974). But cf. *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1, 40 n.26, 42 (1977) (denying disappointed tender of-

equitable remedies will be handled in the same way as implication of damages.

In recent years the Supreme Court has also curbed the implied ancillary remedy of an award of attorneys' fees to a prevailing party. In 1970, in *Mills v. Electric Auto-Lite Co.*, the Court relied on its inherent equitable powers to authorize such awards.<sup>126</sup> In *Alyeska Pipeline Service Co. v. Wilderness Society*<sup>127</sup> in 1975, however, the Court denied attorneys' fees to a successful plaintiff who claimed to be acting as a private attorney general in an environmental suit. Noting that Congress had provided in specific cases for such awards, the Court held that "courts are not free to fashion drastic new rules with respect to the allowance of attorneys' fees."<sup>128</sup> Similarly, the Court has refused to infer a right to contribution among anti-trust defendants<sup>129</sup> or other implied remedies.<sup>130</sup>

Do the cases on implied damage actions and other implied remedies bode drastic restrictions on ancillary relief in administrative law? Implied damage actions are arguably distinguishable from ancillary remedies. Commentators have suggested many policy justifications for limiting implied damage actions. Implied damage actions, which are suits that could not other-

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feror a damage action under the Williams Act, but hinting that an injunction might be available at an early stage). Several pre-*Cort* cases had followed the rationale of *Borak* in awarding injunctive relief. See *Rosado v. Wyman*, 397 U.S. 397 (1970); *Sullivan v. Little Hunting Park, Inc.*, 396 U.S. 229 (1969); *Allen v. State Bd. of Elections*, 393 U.S. 544 (1969); *Jones v. Alfred H. Mayer Co.*, 392 U.S. 409 (1968).

It has been suggested that "[d]amages remedies, especially when created after the fact, often involve harsher results than simple equitable relief, thus indicating a complex balancing of interests best left to the legislature." Note, *supra* note 93, at 393. As the same article concedes, however, this is not invariably true. *Id.* at 393 n.176. Certainly the restructuring of corporate boards through ancillary relief involves harsh results and "a complex balancing of interests."

126. 396 U.S. 375, 389-97 (1970). See *supra* note 109.

127. 421 U.S. 240, 247-71 (1975).

128. *Id.* at 269. The Court distinguished cases like *Mills* on the ground that they involve the creation of a benefit by the plaintiff for a class and that it would be inequitable for the class to share the benefit without sharing the plaintiff's attorneys' fees. *Id.* at 257-58.

129. *Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 639-47 (1981). Although actions for contribution arguably differ from private damage actions, the Court relied on the implied private action cases.

130. *Cf. Southern Pacific Transp. Co. v. Commercial Metals Co.*, 102 S. Ct. 1815 (1982) (consigner of freight may not assert carrier's violation of ICC credit regulations as defense in suit to recover unpaid freight charges); *T.I.M.E. Inc. v. United States*, 359 U.S. 464, 471-72 (1959) (shipper of freight not only may not assert unreasonableness of rates in a damage action but also may not assert it as a defense in action by carrier for past charges).

wise be brought in federal court, contribute to the burgeoning volume of federal litigation that has so concerned the Court recently.<sup>131</sup> Implied damage actions can encourage vexatious nuisance suits brought largely for their settlement value.<sup>132</sup> Such suits may produce "error costs," such as the hindrance of capital formation, and these costs may ultimately be borne by shareholders, whom the securities laws are supposed to protect, without necessarily compensating the victims of the violation of the law.<sup>133</sup> Furthermore, implied damage actions cause confusion by clashing with express remedies and interfering with agency enforcement of regulatory statutes.<sup>134</sup>

To some extent these criticisms do not apply to ancillary relief and, therefore, may justify distinguishing ancillary remedies from other implied remedies. Ancillary remedies create

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131. See *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 102 S. Ct. 1825, 1838-39 (1982) ("the increased volume of federal litigation strongly supported the desirability of a more careful scrutiny of legislative intent" in implied private action cases).

132. Some claim that the breadth and vagueness of rule 10b-5 threaten sizable but unmeasurable damages and, therefore, impel defendants to settle, which in turn encourages the filing of suits brought solely for their settlement value. See Frankel, *supra* note 112, at 573-75. See also *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 739-43 (1975) (purchaser-seller requirement necessary in 10b-5 damage actions to avoid hindrance of defendant's business flowing from the very pendency of such suits and because of the possible abuse of liberal discovery). See also K. ELZINGA & W. BREIT, *THE ANTITRUST PENALTIES: A STUDY IN LAW AND ECONOMICS* 90-95 (1976) (private damage actions under the antitrust laws facilitate nuisance suits brought for settlement value because defendants are risk averse, damages are trebled and juries are irrational).

133. See *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 739-40 (1975) (costs of 10b-5 damage judgments may fall on innocent shareholders); Frankel, *supra* note 112, at 578 (threat of liability hinders capital formation), 580-81 (in class action damages suits many members of the plaintiff class do not actually recover any part of the damage award). Professor Frankel says these "error costs" result in overdeterrence and sees the Supreme Court's restrictions on implication as a response to this overdeterrence. *Id.* at 582.

134. See *Securities Investor Protection Corp. v. Barbour*, 421 U.S. 412, 420-23 (1975), and *National R.R. Passenger Corp. v. Nat'l Ass'n of R.R. Passengers*, 414 U.S. 453, 462-64 (1974), both denying implied private actions in part because they would interfere with discretion vested in a regulatory body. See also *Davis v. Passman*, 442 U.S. 228, 241 (1979) ("Statutory rights and obligations are established by Congress, and it is entirely appropriate for Congress, in creating these rights and obligations, to determine in addition who may enforce them and in what manner."); Frankel, *supra* note 112, at 568-81. Cf. *Southern Pacific Transp. Co. v. Commercial Metals Co.*, 102 S. Ct. 1815 (1982) (judicially created remedy unnecessary because regulations in question could be enforced by regulatory agency).

Even when private damage actions do not hinder agency regulation, they may do no more than "hang on the coattails" of agency actions. Frankel, *supra* note 112, at 579. The primary goal of agency actions, including enforcement actions, is deterrence, but this is not true of private actions. *Id.* at 571.

no new causes of action and do not generally clash with express remedies.<sup>135</sup> More important, most ancillary relief cases are brought by the SEC and therefore do not hamper agency enforcement<sup>136</sup> or have other shortcomings of private damage actions.<sup>137</sup> But to the extent that the criticisms of implied damage actions are well-founded,<sup>138</sup> many of them can also be lev-

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135. The Court has noted a distinction between having a cause of action and being entitled to relief. *Davis v. Passman*, 442 U.S. 228, 239-40 n.18 (1979). The danger of clashing with express remedies depends in part on what express remedies have been provided in the relevant statute and in part on what one means by a "clash." Since the 1933 and 1934 Acts do not expressly forbid the ancillary remedies courts have created as to general issuers, there is in one sense no clash between the express and implied remedies. Congress, however, did provide for certain ancillary remedies in other securities laws and, as to securities professionals, in the 1934 Act, as well. See *infra* notes 161-64 and accompanying text. Thus, it is at least anomalous to create remedies by implication in areas where Congress has not expressly authorized them if Congress has expressly authorized those remedies in related statutes and in other parts of the same statute.

136. Of course, this might not be true in private actions for ancillary relief. See *supra* note 43. It is not clear whether the Court will treat SEC suits differently from private actions. In general, the Court has not distinguished between the two except to the extent indicated by the statutory language. See *Aaron v. SEC*, 446 U.S. 680 (1980) (applying the same standard of culpability to SEC actions as to private actions). Since the securities laws expressly authorize only the SEC to seek an injunction, however, the Court might treat the two differently with respect to ancillary relief.

137. Vesting an administrative agency with enforcement powers may not only conserve judicial resources but also promote enforcement policies that are consistent and informed by expert discretion and concern for the public interest. Private plaintiffs sue not when enforcement is most needed but when the probability of recovery is greatest.

138. Charges that private damage actions encourage nuisance suits have usually been leveled at specific types of claims, and not at private damage actions generally. Thus, *Blue Chip Stamps* concerned only the purchaser-seller requirement under rule 10b-5, and private damage actions under the antitrust laws (which are express, not implied) are unusual because damages are trebled. See *supra* note 132. Although implied private actions undoubtedly do permit some groundless nuisance suits, it is not clear that this problem is vastly greater than it is for express private actions. Nor is it clear that implied private actions produce greater error costs than express actions. See *supra* note 133. Although the threat of 10b-5 liability, for example, may thwart some marginal legitimate transactions, its principal effect should be deterrence of dubious transactions. In so doing, it should facilitate capital formation by promoting investor confidence. Any clash of implied damage actions with express actions, see *supra* note 134, can be avoided by judicially limiting the implied action, as the Supreme Court has done with rule 10b-5. See *infra* notes 206-07. Although implied damage actions may occasionally hinder agency enforcement, the SEC has invariably supported implication in securities law on the ground, accepted by the Court in *J.I. Case Co. v. Borak*, 377 U.S. 426, 432 (1964), that private enforcement is "a necessary supplement to Commission action." This view, never criticized by commentators until the Supreme Court changed directions, makes it difficult to argue that the Court is reacting to overdeterrence.

In sum, these criticisms of implied damage actions, though not without merit, do not adequately explain the Court's drastic restrictions. Indeed, Pro-



eled at ancillary relief. Although ancillary relief creates no new claims, it often complicates cases procedurally.<sup>139</sup> An SEC action for an injunction and ancillary relief pressures a defendant to settle, regardless of the merits, even more than does a private damage action.<sup>140</sup> SEC actions for ancillary relief can also produce error costs, including hindrance of capital formation, and it is the shareholder-investors who will often have to bear these costs.<sup>141</sup>

Although the Supreme Court has not recently discussed ancillary relief in administrative law, some of its holdings and broad dicta suggest that it does not consider implied damage

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fessor Frankel, who offers many of these criticisms, also criticizes the Court's current attitude as much too restrictive. Frankel, *supra* note 112, at 584.

139. In cases involving the appointment of receivers or special counsel or substantial corporate governance changes, *see supra* notes 21, 26-31 and accompanying text, substantial judicial administration is often necessary. *See supra* note 40; *infra* text following note 312; *infra* note 350 and accompanying text. Moreover, although ancillary relief creates no new claims, it may encourage the SEC to sue when, believing an injunction alone unnecessary, it would otherwise not bother to sue.

140. *See infra* notes 372-76 and accompanying text. Although the SEC does not bring meritless suits in pursuit of pecuniary gain, various bureaucratic imperatives may impel it to bring questionable suits. The Commission has been criticized for bringing too many such suits. *See* H. KRIPKE, *THE SEC AND CORPORATE DISCLOSURE* 22-23, 47-51, 283-84 (1979). *See also* R. KARMEL, *REGULATION BY PROSECUTION* 221, 226 (1982) (SEC lacks standards for initiation and prosecution of suits and too often settles hard cases).

Professor Frankel attempts to distinguish actions for equitable relief on the grounds that the courts' discretion prevents overdeterrence in equitable actions. Frankel, *supra* note 112, at 571-72. Aside from the Supreme Court's treatment of private actions for implied equitable remedies the same as implied damage actions, *see supra* notes 124-25 and accompanying text, and the Court's ability to limit implied damage actions, as it has done with 10b-5 cases, *see infra* notes 206-07, judicial discretion in SEC ancillary relief cases is insignificant because most such cases are settled by consent, with the court having little opportunity to exercise discretion as to remedies, *see supra* note 23. *See generally infra* notes 366-79 and accompanying text.

141. Ancillary remedies involving pecuniary relief—restitution, rescission, and disgorgement—are identical to damage actions in their impact on shareholders and in their tendency to deter legitimate transactions. Ancillary remedies affecting corporate governance pose an even greater threat to corporate managements—the loss of corporate control and even removal from corporate office—and therefore produce even more overdeterrence. Such remedies may also come at the expense of shareholders when directors are appointed without shareholder vote, *see infra* notes 313-16 and accompanying text, or when the corporation owned by the shareholders must pay pecuniary relief, *see* *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 739-40 (1975); *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 866-68 (2d Cir. 1968) (Friendly, J., concurring) (courts should hesitate to impose large damage judgments on corporations to detriment of shareholders), 889 (Moore, J., dissenting), *cert. denied*, 394 U.S. 976 (1969); Frankel, *supra* note 112, at 577-78. Ancillary relief also sometimes limits shareholders' rights by immunizing court-appointed directors from liability for negligence. *See infra* note 322 and accompanying text.

actions unique. It has applied the same standards to private actions for equitable relief, for attorneys' fees, and for contribution among defendants, as it has applied to implied damage actions.<sup>142</sup> Many statements by the Court seem to encompass implied ancillary relief as well as other implied remedies.<sup>143</sup>

Moreover, the Court has restricted implied remedies not because of their merits or demerits, but because of the deference due to Congress as to statutory remedies.<sup>144</sup> The Court has stressed that Congress, and not the judiciary, should determine statutory remedies: "The federal judiciary will not engraft a remedy on a statute, no matter how salutary, that Congress did not intend to provide."<sup>145</sup> Even if this principle is not constitutionally mandated by the separation of powers doc-

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142. See *supra* notes 127-33 and accompanying text. Of course, these cases, too, may be distinguishable from ancillary relief cases. *Alyeska Pipeline* reverted to the long tradition in American law that parties pay their own attorneys. Implied private actions for equitable relief or for contribution could facilitate new lawsuits, thereby increasing the burden on the federal courts. Such implied remedies might also produce error costs without necessarily aiding the purposes of the statute.

143. *National R.R. Passenger Corp. v. Nat'l Ass'n of R.R. Passengers*, 414 U.S. 453, 458 (1974) ("when legislation expressly provides a particular remedy or remedies, courts should not expand the coverage of the statute to subsume other remedies"). See *Middlesex County Sewerage Auth. v. Nat'l Sea Clammers Ass'n*, 453 U.S. 1, 15 (1981) ("In the absence of strong indicia of a contrary congressional intent, we are compelled to conclude that Congress provided precisely the remedies it considered appropriate."); *Northwest Airlines, Inc. v. Transport Workers Union*, 451 U.S. 77, 94 n.30 (1981). See also *supra* notes 119-20, *infra* note 145 and accompanying text.

144. See *supra* text accompanying notes 117-20. Thus, cases dealing with constitutional remedies are largely irrelevant. See *supra* note 105 and accompanying text. Indeed, with respect to implied damage actions the Court in recent years has traveled in opposite directions in constitutional and statutory cases, essentially reversing itself in both areas. In statutory cases the Court has gone from a willingness, even eagerness, to infer private damage actions, to a strong reluctance to infer such actions. In constitutional cases, however, the Court had never recognized a private right of action for damages until *Bivens v. Six Unknown Named Agents*, 403 U.S. 388 (1971). In *Carlson v. Green*, 446 U.S. 14 (1980), the Court held that, absent special factors, it will always infer a private damage action for constitutional violations unless Congress has expressly conferred immunity from such action. See also *Cannon v. University of Chicago*, 441 U.S. 677, 733 n.3 (1979) (Powell, J., dissenting) ("[T]he implication of remedies to enforce constitutional provisions does not interfere with the legislative process in the way that implication of remedies from statutes can."). Within the statutory realm the Court may also distinguish between civil rights and economic regulation. See Frankel, *supra* note 112, at 563 n.59; Hazen, *supra* note 109, at 1343-44, 1355; Note, *supra* note 93, at 378. The Court's tradition of protecting minorities may make it less deferential to congressional intent and less demanding that Congress spell out that intent in the civil rights area.

145. *California v. Sierra Club*, 451 U.S. 287, 297 (1981). See *Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 643 (1981), where the Court held that, although it should "give shape to the [Sherman Act's] broad mandate by drawing on common-law tradition," it did not have "as wide discretion in formulat-

trine, as Justice Powell believes,<sup>146</sup> the Court sees Congress as better suited and, under our constitutional system, the preferable body to make the policy decisions entailed in fixing statutory remedies.<sup>147</sup> Congress deserves no less deference as to ancillary remedies in agency actions than it deserves as to other implied remedies. Indeed, the awesome power of government should make judges even more cautious in implying remedies for an administrative agency. It is, therefore, difficult to distinguish ancillary remedies from other implied remedies.

To treat ancillary remedies like other implied remedies would not end ancillary relief, however. Despite its more restrictive attitude, the Court still infers remedies where Congress clearly intended to create them.<sup>148</sup> Consistent with this

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ing remedies." See also *id.* at 646; Frankel, *supra* note 112, at 563-64; *supra* text accompanying notes 119-20; *supra* note 143.

146. Justice Powell believes that Congress has the "constitutional obligation" to specify what actions may be brought under federal statutes and that when this determination is left to the courts "the legislative process with its public scrutiny and participation has been bypassed, with attendant prejudice to everyone concerned." *Cannon v. University of Chicago*, 441 U.S. 677, 743 (1979) (Powell, J., dissenting). *Accord* *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 102 S. Ct. 1825, 1848 (1982) (Powell, J., dissenting); *Bivens v. Six Unknown Named Agents*, 403 U.S. 388, 411-12 (1971) (Burger, C.J., dissenting) (separation of powers dictates that the Court not infer private damage action for violation of Constitution). Former SEC Commissioner Roberta S. Karmel has echoed these sentiments and opined that the implication of ancillary remedies produces the same evils as implication of private rights of action. See *R. KARMEL*, *supra* note 140, at 200-01. Some commentators believe that judicial creation of remedies does not violate the separation of powers if Congress has delegated to the courts the power to do so. See, e.g., Greene, *supra* note 121, at 491, 494. The Supreme Court has rejected the view that such power has been delegated in statutes conferring jurisdiction. *Id.* at 472-73, 477, 487-88, 504. See *supra* note 121 and accompanying text. Nevertheless, the majority of the justices reject Justice Powell's separation of powers argument. See *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 102 S. Ct. 1825, 1837-39 (1982).

147. "Congress has superior capacity to develop the necessary information and to strike the necessary compromises among competing interests." Frankel, *supra* note 112, at 584. Outside the realm of constitutional rights, it is entirely appropriate in a democratic society that remedies be established by the legislature, which can weigh these "competing interests" in the political arena, rather than by the courts, which, in theory at least, ignore political considerations. See Note, *supra* note 93, at 395-96. Legislation also has the merit of operating prospectively, so that persons affected thereby are warned in advance. Legislation can deal with a problem comprehensively while courts are largely limited to dealing with problems one case at a time.

148. See *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 102 S. Ct. 1825 (1982) (inferring private damage action under the Commodity Exchange Act); *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11 (1979) (inferring action for rescission and restitution only); *Cannon v. University of Chicago*, 441 U.S. 677 (1979) (inferring private damage action under Title IX of the Educational Amendments of 1972); *supra* note 124 and accompanying text. See also *Snepp v. United States*, 444 U.S. 507 (1980) (not involving any administrative or other statute; the Court approved, as a matter of federal common law,

approach the Court could approve ancillary remedies that Congress intended. Such remedies must arise from statutory construction, however, not from judicial policy-making under the federal common law.

#### IV. THE SCOPE OF THE FEDERAL SECURITIES LAWS

##### A. THE TEXT AND LEGISLATIVE HISTORY OF THE FEDERAL SECURITIES LAWS

###### 1. *Express Enforcement Powers*

The securities laws expressly grant the SEC many enforcement powers applicable to general issuers. The 1933 and the 1934 Acts both authorize the SEC to seek an injunction against any actual or threatened violation of the respective Act or its rules.<sup>149</sup> Under the 1934 Act, the Commission may also obtain "writs of mandamus, injunctions, and orders commanding . . . any person to comply with" the securities laws and rules.<sup>150</sup> These provisions do not authorize ancillary relief, however.<sup>151</sup>

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the imposition of a constructive trust on the profits earned by a former CIA agent in publishing a book not cleared by the CIA in accordance with the employment agreement between the CIA and the agent).

149. Securities Act of 1933, § 20(b), 15 U.S.C. § 77t(b) (1976); Securities Exchange Act of 1934, § 21(d), 15 U.S.C. § 78u(d) (1976).

150. Securities Exchange Act of 1934, § 21(e), 15 U.S.C. § 78u(e) (1976). Section 20(c) of the 1933 Act, 15 U.S.C. § 77t(c) (1976), is generally to the same effect. Unlike section 21(e) of the 1934 Act, section 20(c) mentions only writs of mandamus, not injunctions and orders. The latter phrase was added to section 21(e) by the Securities Reform Act of 1975. The legislative history does not explain the addition, but it was probably a technical change to reflect the abolition of the writ of mandamus in federal practice. See 3 L. LOSS, *supra* note 57, at 1982. Unlike section 20(c), section 21(e) also permits the SEC to seek an order compelling compliance with the rules of certain self-regulatory organizations or compelling certain such organizations to enforce their own rules.

151. See Farrand, *supra* note 4, at 1780 n.3; Comment, *Texas Gulf Sulphur*, *supra* note 4, at 947 n.21. The language of the statutes themselves suggests this; they provide only for relief commanding "any person to comply" with the law and not for any ancillary remedies. The scant legislative history supports this view. It talks of "commanding any person to comply," H.R. REP. NO. 1383, 73d Cong., 2d Sess. 26 (1934), and "compel[ling] obedience to the act," S. REP. NO. 792, 73d Cong., 2d Sess. 22 (1934). The cases have limited the provisions to this purpose. See *Union Corp. of America v. SEC*, 309 F.2d 93 (8th Cir. 1962) (mandatory injunction compelling defendant to file proper reports); *SEC v. IMC Int'l, Inc.*, 384 F. Supp. 889, 894 (N.D. Tex. 1974) (injunction issued "only to require observance . . . of the federal securities laws"); *SEC v. Transamerica Corp.*, 67 F. Supp. 326, 334 (D. Del. 1946), *modified on other grounds*, 163 F.2d 511 (3d Cir. 1947), *cert. denied*, 332 U.S. 847 (1948) (order to comply with Act by including shareholder proposal in proxy statement); *SEC v. Nevada Oil Co.*, 5 SEC Jud. Dec. 5 (N.D. Tex. 1946) (mandatory injunction directing defendant corporation to make corporate books and records available to plaintiff for reasonable inspection); *SEC v. Sharkey*, 4 SEC Jud. Dec. 574 (W.D. Wash. 1945) (order compelling defendant to make books available to the SEC). Congress

Nor do the securities laws' provisions conferring jurisdiction<sup>152</sup> create any remedy.<sup>153</sup> Section 16 of the 1933 Act and section 28(a) of the 1934 Act,<sup>154</sup> which provide that the rights and remedies in these Acts are "in addition to any and all other rights and remedies that may exist at law or in equity," merely negate any implied preemption of state law; they provide no basis for ancillary relief.<sup>155</sup>

Other remedies available against general issuers include stop orders and orders to suspend trading or to suspend a registration statement.<sup>156</sup> Of late the SEC has used its power to publicize findings from an investigation<sup>157</sup> with the aim, according to some critics,<sup>158</sup> of punishing persons who engage in conduct the Commission does not like. The Commission may subpoena witnesses, compel preparation of documents, and conduct investigations,<sup>159</sup> and may also refer a case to the At-

may have added these provisions to the injunctive provisions for fear that the latter might be construed to permit the courts only to forbid certain acts and not to command the performance of an act.

152. 15 U.S.C. §§ 77v(a), 78aa (1976).

153. See *supra* notes 121-22 and accompanying text. Cf. *supra* text accompanying notes 49, 111.

154. Securities Act of 1933, § 16, 15 U.S.C. § 77p (1976); Securities Exchange Act of 1934, § 28(a), 15 U.S.C. § 78bb(a) (1976).

155. Independence Shares Corp. v. Deckert, 108 F.2d 51, 54 (3d Cir. 1939), *rev'd on other grounds*, 311 U.S. 282 (1940). The author is not aware of any case that has used either of these provisions to justify any additional remedy except pursuant to state law. The Supreme Court has found it unlikely that similar statutory language was intended to include other remedies under the same statute. See *Middlesex County Sewerage Auth. v. Nat'l Sea Clammers Ass'n*, 453 U.S. 1, 15-16 (1981).

156. Securities Act of 1933, § 8, 15 U.S.C. § 77h (1976); Securities Exchange Act of 1934, §§ 12(j)-12(k), 15 U.S.C. §§ 78l(j)-(k) (1976) (suspension of trading and temporary, summary suspension of trading). Securities Act of 1933, § 8(d), 15 U.S.C. § 77h(d) (1976) (suspension of 1933 Act registration statement); Securities Exchange Act of 1934, § 12(j), 15 U.S.C. § 78l(j) (1976) (suspension of 1934 Act registration statement).

157. Securities Exchange Act of 1934, §§ 15(c)(4), 21(a), 15 U.S.C. §§ 78o(c)(4), 78u(a) (1976).

158. Professor Kripke has spoken of "the punishment of publicity" and noted that by use of this power the SEC avoids questions of its jurisdiction to intervene in particular matters and even avoids having to find or to charge a violation of law. See Kripke, *The SEC, Corporate Governance, and the Real Issues*, 36 BUS. LAW. 173 (1981). Professor Davis has also called adverse publicity an SEC sanction. See K. DAVIS, *ADMINISTRATIVE LAW* 446 (3d ed. 1972).

159. Securities Act of 1933, §§ 8(e), 19(b), 20(a)-(b), 15 U.S.C. §§ 77h(e), 77s(b), 77t(a)-(b) (1976); Securities Exchange Act of 1934, §§ 17(a), 21(a)-(b), 15 U.S.C. §§ 78q(a), 78u(a)-(b) (1976); Investment Company Act of 1940, §§ 14(b), 31(a)-(b), 42(a)-(b), 15 U.S.C. §§ 80a-14(b), 80a-31(a)-(b), 80a-42(a)-(b) (1976); Investment Advisers Act of 1940, § 209(a), (e), 15 U.S.C. § 80b-9(a), (e) (1976).

It has been suggested that the SEC assist private enforcement by procuring judgments which private plaintiffs can use as a basis for offensive collateral estoppel. See Hazen, *supra* note 25, at 451-60.

torney General for criminal prosecution.<sup>160</sup> Nothing in either act expressly permits, or strongly implies permission to pursue, the ancillary remedies that the SEC has often obtained against general issuers.

Even in the area of securities law Congress has not always been so reticent about ancillary relief. The Investment Company Act and the Investment Advisers Act<sup>161</sup> both permit court appointment of a trustee to control the defendant's business. The Investment Company Act also permits a court to bar from any office in an investment company, and to "award . . . injunctive or other relief" against, any person guilty of "a breach of fiduciary duty involving personal misconduct."<sup>162</sup> These remedies reflect the function of the Investment Company Act as a federal corporation law for investment companies,<sup>163</sup> which contrasts sharply with the more limited regulation of the securities acts. Even in the 1934 Act, as amended, Congress authorized the SEC to regulate the internal affairs of firms in the securities industry, including broker-dealers and securities exchanges.<sup>164</sup> Elsewhere, Congress has authorized administrative agencies to request similar relief.<sup>165</sup>

These broader statutes suggest that when Congress wanted

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160. Securities Act of 1933, § 20(b), 15 U.S.C. § 77t(b) (1976); Securities Exchange Act of 1934, § 21(d), 15 U.S.C. § 78u(d) (1976); Investment Company Act of 1940, § 42(e), 15 U.S.C. § 80a-43(e) (1976); Investment Advisers Act of 1940, § 209(e), 15 U.S.C. § 80b-9 (1976).

161. 15 U.S.C. § 80b-9(e) (1976).

162. 15 U.S.C. § 80a-35(a) (1976) (emphasis added). See *Bailey v. Proctor*, 160 F.2d 78 (1st Cir.), cert. denied, 331 U.S. 834 (1947); *SEC v. Wong*, 252 F. Supp. 608 (D.P.R. 1966).

163. "In certain major respects, the 1940 Act operates as a corporation law for investment companies. In sharp contrast, the 1934 Act . . . regulates one phase,—the purchase and sale of corporate securities." *Brown v. Bullock*, 194 F. Supp. 207, 232-33 (S.D.N.Y.), *aff'd without consideration of this point*, 294 F.2d 415 (2d Cir. 1961). The 1940 Act regulates investment companies on many matters of internal governance that are left to state law with respect to industrial companies. See Fleischer, "Federal Corporation Law": An Assessment, 78 HARV. L. REV. 1146, 1153 n.38 (1965).

164. The SEC is empowered to suspend or revoke the registration, or to censure or impose limitations upon the activities, functions, and operations of national stock exchanges, registered securities associations, broker-dealers and other regulated entities, and may similarly discipline members or officials thereof and persons associated therewith. 15 U.S.C. §§ 78o(b)(4), (6), 78s(h) (1976). The Commission has similar powers as to investment companies and investment advisors. 15 U.S.C. §§ 80a-9(b), 80b-3(e)-(f) (1976). In case of the suspension or revocation of the registration of a clearing agency, a court may be petitioned for the appointment of a trustee. 15 U.S.C. § 78s(i) (1976). The Commission also has power to disapprove, abrogate, or amend the rules of stock exchanges, securities associations, etc. 15 U.S.C. § 78s(b)-(c) (1976).

165. See *supra* notes 62, 63, 65 and accompanying text.

to authorize ancillary remedies, it knew how to do so and, therefore, that when Congress omitted such remedies, it intended not to authorize them. In the last few years the Supreme Court has often followed this rationale in refusing to imply or to expand private damage actions or other remedies.<sup>166</sup> This principle is especially compelling as to relief affecting corporate governance. Congress expressly empowered the SEC to regulate the governance of firms in the securities industry, but in the same and related statutes withheld such powers with respect to general issuers. The reasonable inference, especially since both securities acts were drafted with extreme care,<sup>167</sup> is that Congress intended not to confer such powers with respect to general issuers.

On occasion the SEC has argued, and could be expected to argue as to ancillary relief, that knowing congressional acquiescence legitimates agency practices which might otherwise be questioned. The Supreme Court has rejected that argument recently,<sup>168</sup> and would probably do so with respect to ancillary relief as well, especially remedies affecting corporate governance,

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166. In *Touche Ross & Co. v. Redington*, 442 U.S. 560, 571-72 (1979), the Supreme Court declined to infer a private right of action under section 17(a) of the 1934 Act, in part because "it is flanked by provisions . . . that explicitly grant private causes of action . . . . Obviously, then, when Congress wished to provide a private damages remedy, it knew how to do so and did so expressly." See *Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 641 n.11 (1981) (express provision in several federal statutes for contribution among defendants suggests lack of congressional intent to require contribution where not expressly provided); *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 21 (1979) (quoting the same passage from *Touche Ross*); *United States v. Testan*, 424 U.S. 392, 404 (1976) (court would not judicially create right to back pay for federal employee improperly classified because to do so would render "carefully limited" statutory scheme "superfluous"); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 734 (1975) ("When Congress wished to provide a remedy to those who neither purchase nor sell securities, it had little trouble in doing so expressly."); *supra* notes 119, 128, 143, 145 and accompanying text.

167. See *Ruder, Civil Liability Under Rule 10b-5: Judicial Revision of Legislative Intent?*, 57 Nw. U.L. Rev. 627, 647-48 (1963).

168. See *Aaron v. SEC*, 446 U.S. 680, 694 n.11 (1980) (where congressional consideration was addressed principally to other matters, "the failure of Congress to overturn the Commission's interpretation [fell] far short of providing a basis to support a construction of § 10(b) so clearly at odds with its plain meaning and legislative history"); *SEC v. Sloan*, 436 U.S. 103, 119-21 (1978) (even approval of Commission's practice in Committee Report and a few statements in legislative history did not suffice where practice "not only is at odds with the language of the section in question and the pattern of the statute taken as a whole, but also is extremely far reaching in terms of the virtually untrammelled and unreviewable power it would vest in a regulatory agency"). But see *Herman & MacLean v. Huddleston*, 103 S. Ct. 683 (1983) (10b-5 action not precluded merely because alleged violation might give rise to claim under § 11). Congress's failure to forbid the SEC's practice is not conclusive where, as here, there has been no affirmative congressional support for the practice, the prac-

because such remedies are a recent phenomenon in which Congress cannot yet be deemed to have acquiesced.

## 2. *Implied Remedies—The Legislative History and Purposes of the Federal Securities Laws*

The securities laws grew out of a national economic crisis. Inquiry into the stock market crash of 1929 uncovered many objectionable practices in the sale of securities and governance of public corporations.<sup>169</sup> Congress intended the securities laws to ameliorate these problems substantially.<sup>170</sup> The House Report stated that the 1933 Act's civil liabilities "would alter corporate organization and corporate practices in this country."<sup>171</sup> The 1934 Act provided substantial substantive regulation of the internal affairs of some segments of the securities industry.<sup>172</sup> Outside the securities industry, however, Congress focused primarily on manipulation in the sale of securities and abuse of the proxy mechanism.<sup>173</sup> Following an approach advocated by such corporate critics as Louis Brandeis,<sup>174</sup> Congress tackled

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tice contradicts the language and legislative history of the securities laws, and the practice would confer awesome power on the Commission.

169. See Anderson, *The Disclosure Process in Federal Securities Regulation: A Brief Review*, 25 HASTINGS L.J. 311, 316-18 (1974); Sommer, *supra* note 24, at 116-20; *infra* note 193 and accompanying text.

170. See Fleischer, *supra* note 163, at 1174-75. Courts have often noted the broad remedial purposes of the securities laws. See, e.g., *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 151 (1972); *SEC v. Capital Gains Research Bureau*, 375 U.S. 180, 195 (1963). The Supreme Court has cautioned, however, that general remedial purposes do not warrant reading the securities laws "more broadly than [their] language and the statutory scheme permit." *SEC v. Sloan*, 436 U.S. 103, 116 (1978). See also *Aaron v. SEC*, 446 U.S. 680, 695 (1980) (quoting *Touche Ross & Co. v. Redington*, 442 U.S. 560, 578 (1979)).

171. H.R. REP. NO. 85, 73d Cong., 2d Sess. 5 (1933). The Report also stated that "all those responsible for statements upon the face of which the public is solicited to invest its money shall be held to standards like those imposed upon a fiduciary." *Id.*

172. See *supra* note 164 and accompanying text. See also Securities Exchange Act of 1934, §§ 6 (conditions for registration of securities exchanges), 7 (margin requirements), 8 (restrictions on borrowing by broker-dealers, the "net capital" requirements), 11 (prohibitions on certain trading activities of broker-dealers), 19 (regulation of self-regulatory organizations), 15 U.S.C. §§ 78f-h, k, s (1976).

173. The basic policy of the 1933 Act was "of informing the investor of the facts concerning securities to be offered for sale in interstate and foreign commerce and providing protection against fraud and misrepresentation." S. REP. NO. 47, 73d Cong., 1st Sess. 1 (1933).

174. "Sunlight is said to be the best of disinfectants; electric light the most efficient policeman." L. BRANDEIS, *OTHER PEOPLE'S MONEY* 92 (1913). Following enactment of the 1934 Act, both Felix Frankfurter and William O. Douglas lauded disclosure as a technique for improving corporate governance. See Weiss & Schwartz, *Using Disclosure to Activate the Board of Directors*, 41 LAW &



both problems by "implementing a 'philosophy of full disclosure,'"<sup>175</sup> intending that the securities laws' impact on corporate governance be indirect, a result of disclosure rather than of direct federal regulation of corporate managements. As to proxy solicitations, this philosophy required disclosure by managements of "their interest and . . . of the management policies they intend to pursue" so as to achieve the goal of "[f]air corporate suffrage."<sup>176</sup> Congress rejected suggestions that the federal government judge the fairness of securities transactions, the suitability of securities offerings, or the merits of proxy contests.<sup>177</sup>

The principal objection directed against the provisions for corporate reporting is that they constitute a veiled attempt to invest a governmental commission with the power to interfere in the management of corporations. The committee has no such intention, and feels that the bill furnishes no justification for such an interpretation.<sup>178</sup>

To stress this point the Senate bill in 1933 expressly forbade "the Commission to interfere with the management of the af-

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CONTEMP. PROBS. 63, 66-67 (Summer 1977). All three deeply influenced the federal securities laws. See 1 L. LOSS, *supra* note 57, at 123-26.

175. *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 477 (1977), discussed in greater detail *infra* at notes 228-40 and accompanying text. See 1933 Act, preamble ("To provide full and fair disclosure of the character of securities . . . and to prevent frauds in the sale thereof, and for other purposes."); Anderson, *supra* note 169, at 318; Knauss, *A Reappraisal of the Role of Disclosure*, 62 MICH. L. REV. 607, 607-10 (1964).

176. "Fair corporate suffrage is an important right that should attach to every equity security . . ." H.R. REP. NO. 1383, 73d Cong., 2d Sess. 13 (1934). The goal was to "prevent . . . the recurrence of abuses which have frustrated the free exercise of the voting rights of stockholders." *Id.* at 14. See *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375, 381 (1970); *J.I. Case Co. v. Borak*, 377 U.S. 426, 431 (1964); S. REP. NO. 1455, 73d Cong., 2d Sess. 74-77 (1934).

177. Congress designed the disclosure requirements of the securities laws so that neither action nor inaction by the Commission could be construed as approval of any security. H.R. REP. NO. 85, 73d Cong., 1st Sess. 3-4 (1933). The House Report stated that "the grant of control to the Federal Trade Commission [the agency responsible for the securities laws before establishment of the SEC by the 1934 Act] conveys with it no right to pass upon the merits of any security, but simply to insist that whatever its merits, facts essential to its character are to be disclosed." *Id.* at 4. *Accord* S. REP. NO. 47, 73d Cong., 1st Sess. 2 (1933). President Roosevelt stated that "[o]f course, the Federal Government cannot and should not take any action which might be construed as approving or guaranteeing that newly issued securities are sound . . . . There is, however, an obligation on us to insist that every issue of new securities . . . shall be accompanied by full publicity and information." S. REP. NO. 47 at 6-7, H.R. REP. NO. 85 at 1-2, 73d Cong., 1st Sess. (1933). See 1 L. LOSS, *supra* note 57, at 121-29; Landis, *The Legislative History of the Securities Act of 1933*, 28 GEO. WASH. L. REV. 29, 30-31, 34 (1959). See also H. KRIPKE, *supra* note 140, at 37-39; Anderson, *supra* note 169, at 318-20; Gadsby, *Historical Development of the SEC—The Government View*, 28 GEO. WASH. L. REV. 6, 9 (1959).

178. S. REP. NO. 792, 73d Cong., 2d Sess. 10 (1934).

fairs of an issuer."<sup>179</sup> The House-Senate conference omitted this clause "as unnecessary, since it is not believed that the bill is open to misconstruction in this respect."<sup>180</sup> This is consistent with President Roosevelt's statement that "[t]he purpose of the legislation I suggest is to protect the public with the least possible interference to honest business."<sup>181</sup>

There are some exceptions to the disclosure approach.<sup>182</sup> The original exceptions, however, were narrow, specific, and clearly contemplated by the Act and its legislative history. Amendments to the securities laws have not changed their fundamental purpose. In particular the Foreign Corrupt Practices Act (FCPA),<sup>183</sup> goes a step beyond the original 1934 Act in that it not only requires corporate disclosure but also mandates certain steps to generate information for disclosure. The FCPA, however, does not authorize the SEC to regulate internal corporate affairs, except to require compliance with the specific provisions of the Act.<sup>184</sup> Indeed, the FCPA underscores in two

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179. *Id.* at 10, 20.

180. H.R. REP. NO. 1838, 73d Cong., 2d Sess. 35 (1934) (Conference Report). See S. REP. NO. 47, 73d Cong., 1st Sess. 1 (1933): "It is the conviction of the committee that [the aims of the 1933 Act] may be largely achieved upon the basis of fidelity to truth." See also Sommer, *supra* note 24, at 118 ("Congress appeared to eschew the use of disclosure as a regulatory mechanism, that is, the use of disclosure to modify corporate conduct."); Disclosure Policy Study (Wheat Report) 10 (1969) ("[T]he draftsmen of the '33 and '34 Acts viewed [the] responsibility [of the Federal government in investment matters] as being primarily one of seeing to it that investors and speculators had access to enough information to enable them to arrive at their own rational decisions.").

181. S. REP. NO. 47 at 7, H.R. REP. NO. 85 at 2, 73d Cong., 1st Sess. (1933). The President's statement refers to "full publicity and information" and "the whole truth." Statements from several Congressmen and others reflect similar concepts. See Ruder, *supra* note 167, at 648 & n.112.

182. Controlling persons are forbidden to profit from short-swing trading. Securities Exchange Act of 1934, § 16(b), 15 U.S.C. § 78p(b) (1976). The SEC's power to regulate proxies goes beyond requiring full disclosure. See Loomis & Rubman, *Corporate Governance in Historical Perspective*, 8 HOFSTRA L. REV. 141, 171 & n.115 (1979).

183. 15 U.S.C. §§ 78m, 78dd-1, 78dd-2, 78ff (Supp. V 1981). The Act requires public issuers to maintain adequate internal accounting controls and to keep adequate records.

184. Of course, the usual remedies available to the Commission, including whatever ancillary remedies are generally appropriate, are available for violations of the FCPA, but the FCPA does not warrant any broader intrusion by the Commission into corporate governance. In hearings on the proposed Act Senator Proxmire stated it "would merely codify the requirement that a corporation keep honest records . . ." *Prohibiting Bribes to Foreign Officials: Hearings on S.3133, S.3379 and S.3418 Before the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 2d Sess. 1 (1976). Senator Tower stated that the Act "would not expand the authority of the SEC nor distort the existing system of corporate self-regulation." SENATE COMM. ON BANKING, HOUSING AND URBAN AFFAIRS, CORRUPT PRACTICES BY U.S. ENTERPRISES, S. REP. NO. 1031, 94th Cong.,

ways Congress's intent to avoid direct intrusion into corporate governance. First, it suggests that the SEC previously lacked power to require what the Act demands; otherwise the Act would be redundant.<sup>185</sup> Further, by this limited extension of the disclosure philosophy of the 1934 Act into corporate governance, Congress implicitly eschewed any more general extension.<sup>186</sup> Although some legislative history of the FCPA suggests support for ancillary relief, it does not demonstrate broad congressional approval.<sup>187</sup>

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2d Sess. 11 (1976). These statements were not challenged during the congressional hearings or debates. Siedel, *Internal Accounting Controls Under the Foreign Corrupt Practices Act: A Federal Law of Corporations?*, 18 AM. BUS. L.J. 443, 458 (1981). See *id.* at 461, 474. See also Baker & Cheramy, *Accounting Practices Under the Foreign Corrupt Practices Act*, 36 BUS. LAW. 733, 736 (1981) (comments of Joseph Hinsey IV, Esq.) ("in my view, the legislation was clearly geared, in terms of what the Congress thought it was doing, to fixing the foreign bribery problem"); *id.* at 742-43. But cf. *Foreign Corrupt Practices Act of 1977 and the Regulation of Questionable Payments*, 34 BUS. LAW. 623, 625 (1979) (comments of Kenneth J. Bialkin, Esq.) (FCPA may be "the jurisdictional hook which may be employed for a more direct involvement by the Commission in the internal operations of issuer corporations."); SEC Securities Exchange Act Release No. 15,570, [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,959, at 81,395 (Feb. 15, 1979) (the accounting provisions of the FCPA concern more than just financial statements; "[a]n equally important objective . . . is the goal of corporate accountability").

185. Legislatures do not generally enact redundant legislation. Moreover, the SEC eagerly sought enactment of the FCPA. See ABA Committee on Corporate Law and Accounting, *A Guide to the New Section 13(b)(2) Accounting Requirements of the Securities Exchange Act of 1934*, 34 BUS. LAW. 307, 328-31 (1978). This suggests that the Commission was at least uneasy about its own powers prior to the FCPA. The Commission has recognized that the FCPA imposes new obligations. SEC Securities Exchange Act Release No. 14,478, [Accounting Series Releases Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 72,264, at 62,701 (Feb. 16, 1978). The legislative history of the FCPA contains some evidence that Congress did not consider its accounting provisions to be a major departure from existing law. See S. REP. NO. 1031, 94th Cong., 2d Sess. 11 (1976) (the accounting provisions of the FCPA are "implicit in the existing securities laws"). The SEC has often expressed similar views. See *Foreign Corrupt Practices Act and the Regulation of Questionable Payments*, 34 BUS. LAW. 623, 657 (1979) (comments of Ralph C. Ferrara, Esq., then Executive Assistant to the Chairman of the SEC) ("I do not think that the accounting provisions of the [FCPA] are materially different from the authority that the Commission has under the other provisions of the Exchange Act."). Cf. SEC Securities Exchange Act Release No. 15,570, [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,959, at 81,395 (Feb. 15, 1979) (SEC says certain rules are being adopted not in reliance on its power under FCPA alone); SEC Securities Exchange Act Release No. 13,185, [1976-77 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,896, at 87,378 (Jan. 19, 1977) (same concerning certain rule proposals).

186. This follows not only from the maxim *expressio unius est exclusio alterius* (which the Supreme Court has often followed recently, see Note, *supra* note 90, at 895 n.28), but also from statements in the legislative history that the FCPA would merely require "honest records" and "would not expand the authority of the SEC." See *supra* note 184.

187. The House Report states: "The Commission, of course, will retain the

Congress's express retention of a broad role for state law underscores its intent to avoid direct regulation of corporate governance. Congress did not confront a regulatory vacuum in 1933-34. There was a long history of state regulation of securities and an even longer history of regulation of corporations. Both the 1933 and 1934 Acts preserve the jurisdiction of state securities commissions,<sup>188</sup> and the legislative history recognizes that the federal securities laws "supplement and strengthen State laws."<sup>189</sup> Under this dual regulation state law prevails unless it clearly conflicts with the manifest intent of Congress.<sup>190</sup> As Professor Loss has noted, "If Congress had intended to give the Commission power to reallocate functions between [directors and shareholders], so revolutionary a federal intervention would presumably have been more clearly expressed."<sup>191</sup>

Finally, congressional rejection of federal incorporation laws before, during, and after 1933-34 evidences Congress's desire to avoid direct regulation of corporate governance. Proposals for federal incorporation of public companies date to the 1880's and reappeared often before 1933.<sup>192</sup> In 1933-34 Congress well understood the concept of federal incorporation. The congressional hearings during that session referred repeatedly to

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power to seek all of the existing equitable remedies that have been recognized by the courts under the securities laws, and the Committee anticipates that the Commission will continue to tailor remedies to fit the circumstances of specific cases." H.R. REP. NO. 640, 95th Cong., 1st Sess. 10 (1977). The Senate Report states that "The Commission, of course, will retain all of its existing remedies under the securities laws, and the committee anticipates that the Commission will continue to tailor remedies to fit the circumstances of specific cases." S. REP. NO. 114, 95th Cong., 1st Sess. 12 (1977). Both statements, and especially the statement in the Senate Report, are somewhat ambiguous because the SEC does have other express remedies apart from implied, ancillary equitable remedies. Also, the Senate Report says that "the only remedy [the SEC] can bring on its own is an injunctive action." *Id.* at 11. This is especially significant because the Senate bill was passed in lieu of the House bill. See 1977 U.S. CODE CONG. & AD. NEWS 4098. Moreover, even the House Report speaks of "existing equitable remedies" (emphasis added). Whether certain remedies, especially those affecting governance, existed then was unclear.

188. 15 U.S.C. § 77r (1976); 15 U.S.C. § 78bb(a) (1976). See 1 L. LOSS, *supra* note 57, at 155-58.

189. *A Study of the Economic and Legal Aspects of the Proposed Federal Securities Act*, in *Federal Securities Act: Hearings on H.R. 4314 Before the House Interstate and Foreign Commerce Committee*, 73d Cong., 1st Sess. 101 (1933). See also H.R. REP. NO. 85, 73d Cong., 1st Sess. 10-11 (1933). See 1 L. LOSS, *supra* note 57, at 155-58; 6 *id.* at 2291-94.

190. See *infra* notes 223-40 and accompanying text.

191. 2 L. LOSS, *supra* note 57, at 902-03.

192. See 1 *id.* at 107-11; Loomis & Rubman, *supra* note 182, at 158-64.

the failures of corporate directors,<sup>193</sup> and some witnesses argued that disclosure alone was inadequate and that federal incorporation was necessary.<sup>194</sup> Nevertheless, Congress deliberately rejected federal incorporation, with its direct regulation of corporate governance, "and opted instead for a more limited approach."<sup>195</sup> After 1934 members of Congress and commentators continued to advocate federal incorporation.<sup>196</sup> Their proposals indicate the limitations that contemporaries saw in the securities laws.<sup>197</sup> Although Congress never adopted federal incorporation, it did subsequently decide to regulate directly the governance of companies in certain industries, such as the mutual fund industry.<sup>198</sup> When Congress wanted to preempt state law as to corporate governance, it ex-

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193. See Sommer, *supra* note 24, at 120-21; authorities cited *supra* note 169.

194. These witnesses included Richard Whitney, president of the New York Stock Exchange, Frank Altschul, chairman of the Exchange's Stock List Committee, and Alfred L. Bernheim of the Twentieth Century Fund. See *Stock Exchange Practices: Hearings Before the Senate Comm. on Banking and Currency*, 73d Cong., 1st Sess. 6709, 6715-16 (Whitney), 6677-78 (Altschul), 6936, 6939-40 (Bernheim) (1933) (cited in Loomis & Rubman, *supra* note 182, at 166 n.94).

195. Loomis & Rubman, *supra* note 182, at 161.

196. For articles proposing federal incorporation or discussing other proposals see Berlack, *Federal Incorporation and Securities Regulation*, 49 HARV. L. REV. 396 (1936); Brown, *The Federal Incorporation Licensing Bill: Corporate Regulation*, 27 GEO. L.J. 1092 (1939); Douglas, *Directors Who Do Not Direct*, 47 HARV. L. REV. 1305, 1314-15 (1934); Jennings, *Federal Incorporation or Licensing of Interstate Corporate Business*, 23 MINN. L. REV. 710 (1939); Reuschlein, *Federalization—Design for Corporate Reform in a National Economy*, 91 U. PA. L. REV. 91 (1942); Watkins, *Federalization of Corporations*, 13 TENN. L. REV. 89 (1935). See also 1 L. LOSS, *supra* note 57, at 109-11. Efforts to enact a federal corporations law continue to this day. See 126 CONG. REC. S3751-52 (daily ed. Apr. 16, 1980) (remarks of Sen. Metzenbaum).

197. Some commentators criticized the securities laws as inadequate to deal with the problems of corporate governance. See Reuschlein, *supra* note 196, at 107-08; TEMPORARY NATIONAL ECONOMIC COMMITTEE, FINAL REPORT AND RECOMMENDATIONS, S. DOC. NO. 35, 77th Cong., 1st Sess. 29 (1941). Some recommended a statutory requirement that corporate boards have a majority of outside directors. See Douglas, *supra* note 196, at 1314-15; M. DIMOCK & H. HYDE, BUREAUCRACY AND TRUSTEESHIP IN LARGE CORPORATIONS 134-35 (TNEC Monograph No. 11, 1940). It is significant that they thought such legislation necessary since in recent years the SEC has often obtained court orders imposing such a requirement as ancillary relief. See *supra* notes 23-25 and accompanying text. As one commentator said, "Congress has not, as yet, made an effort to exercise any substantial degree of control over the internal affairs of corporations engaged in interstate commerce." Berlack, *supra* note 196, at 410.

198. See *supra* notes 161-62 and accompanying text. See also Fleischer, *supra* note 163, at 1153 n.38; Sommer, *supra* note 24, at 119-20 (contrasting the Investment Company Act's regulation of internal corporate affairs with the absence of such regulation in the 1933 and 1934 Acts).

pressed its intent clearly.<sup>199</sup>

Although the foregoing discussion of legislative history concerns the scope of SEC regulation, the principles developed there apply equally to remedies. Congress does not always intend the broadest possible remedies; in the securities laws Congress deliberately limited certain remedies so as to avoid injury to "honest business."<sup>200</sup> Interference with "fair corporate suffrage" and corporate governance and state regulation thereof can arise as much from court-ordered remedies as from direct SEC regulation.<sup>201</sup> Nor did Congress intend to permit federal intrusion into corporate governance once a corporation has violated the securities laws. If Congress had intended such a major exception to the general rule of noninterference in corporate governance, presumably it would have said so, as it did in other securities laws and statutes in other areas.<sup>202</sup> Most reasons for Congress's renunciation of direct regulation of corporate governance are as valid for judicial remedies as for SEC rule-making.<sup>203</sup>

In sum, although the legislative history of the securities laws does not discuss ancillary relief, it does evince a clear congressional intent not to regulate corporate governance unless an express statutory provision applies,<sup>204</sup> or unless disclosure requirements are implicated.

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199. See *supra* text accompanying note 191. *Edgar v. MITE Corp.*, 102 S. Ct. 2629 (1982), is not to the contrary. See *infra* note 231.

200. See H.R. REP. NO. 85, 73d Cong., 1st Sess. 9-10 (1933) (restricting plaintiffs under §§ 11-12 of the 1933 Act to recovery of the offering price). See also § 206(d) of the 1934 Act, 48 Stat. 907-08 (amending § 11 of the 1933 Act to limit damages recoverable).

201. See *supra* note 39 and accompanying text (ancillary relief has involved removing and appointing directors without any shareholder vote); *infra* notes 312-20 and accompanying text.

202. See *supra* notes 161-65 and accompanying text.

203. See *infra* notes 323-24 and accompanying text. If the prohibition on direct regulation of corporate governance is due solely to the assumption that most businesses are honest and do not need such regulation, arguably the prohibition should not apply in any case in which the assumption is proved wrong by a violation of the securities laws. As the preceding discussion shows, however, Congress avoided such regulation because it wanted to leave that task to state law and to shareholder suffrage. Interference with corporate governance by ancillary relief, therefore, violates congressional intent as much as would an SEC rule to the same effect. In fact, ancillary relief may be an even greater violation because shareholders and state governmental representatives ordinarily cannot participate as easily in a judicial proceeding as in a rule-making proceeding.

204. See *supra* notes 182-83 and accompanying text.

## B. RECENT JUDICIAL RESTRICTIONS

Implication of private rights of action<sup>205</sup> is not the only area in which the Supreme Court has limited the federal securities laws.<sup>206</sup> The Court has also restricted enforcement actions,<sup>207</sup> the tender offer laws and rules,<sup>208</sup> section 16(b) of the 1934 Act,<sup>209</sup> the definition of the term "security,"<sup>210</sup> and other provisions of securities laws.<sup>211</sup>

SEC enforcement cases are especially instructive. In *Aaron v. SEC*<sup>212</sup> the Supreme Court upheld a negligence standard for injunctions under sections 17(a)(2) and 17(a)(3) of the 1933 Act but also imposed on the SEC the same scienter stan-

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205. See *supra* notes 107-48 and accompanying text.

206. Although the Court still recognizes private causes of action under rule 10b-5, it has stressed that, because they are judicially implied, it may limit 10b-5 claims as policy considerations require, *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 748-49 (1975), and has often done just that, see *Chiarella v. United States*, 445 U.S. 222 (1980) (10b-5 imposes no affirmative duty to disclose absent some fiduciary relationship); *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462 (1977) (discussed *infra* notes 228-40 and accompanying text); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976) (scienter required for 10b-5 civil damage action); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975) (10b-5 plaintiff must be a purchaser or seller).

207. See *Aaron v. SEC*, 446 U.S. 680 (1980) (discussed *infra* notes 212-13 and accompanying text). But see *Steadman v. SEC*, 450 U.S. 91 (1981) (discussed *infra* note 224).

208. See *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1 (1977) (no private damage action for disappointed tender offeror); *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 60-65 (1975) (no injunction for violation of Williams Act absent proof of irreparable harm).

209. See *Foremost-McKesson, Inc. v. Provident Secs. Co.*, 423 U.S. 232 (1976) (one need account for profit on sale of shares only if one was a 10% owner before purchasing); *Kern County Land Co. v. Occidental Petroleum Corp.*, 411 U.S. 582 (1973) (exchange of shares through tender offer which defendant could not prevent not deemed a § 16(b) sale).

210. See *Marine Bank v. Weaver*, 102 S. Ct. 1220 (1982) (certificate of deposit and a contractual arrangement are not securities); *International Bhd. of Teamsters v. Daniel*, 439 U.S. 551 (1979) (interest in an involuntary, noncontributory pension plan is not a security); *United Housing Found. v. Forman*, 421 U.S. 837 (1975) (shares in a housing cooperative are not securities). But cf. *Rubin v. United States*, 449 U.S. 424 (1981) (discussed *infra* note 224).

211. See *Burks v. Lasker*, 441 U.S. 471 (1979) (power of directors of investment company to terminate derivative suit is to be decided by state law unless it clearly conflicts with federal law); *SEC v. Sloan*, 436 U.S. 103 (1978) (discussed *infra* notes 214-22 and accompanying text); *TSC Indus., Inc. v. Northway*, 426 U.S. 438 (1976) (narrowing definition of term "materiality"). But cf. *United States v. Naftalin*, 441 U.S. 768 (1979) (discussed *infra* note 224).

212. 446 U.S. 680 (1980). The holding was based primarily on the express language of the relevant statutes. Moreover, the Court took pains to note that the holding that sections 17(a)(2) and (a)(3) do not require scienter might not be very important because scienter would still be important to the trial court's decision whether to issue an injunction. *Id.* at 701. In subsequent cases lower courts have declined to issue injunctions for want of scienter under sections 17(a)(2) and (a)(3). See, e.g., *SEC v. Haswell*, 654 F.2d 698 (10th Cir. 1981).

dard in injunctive proceedings under section 17(a)(1) and rule 10b-5 that applies to a private plaintiff in a civil damage action. The Court also indicated that to obtain an injunction the SEC must show a reasonable likelihood of future violations if the injunction is not issued.<sup>213</sup>

In *SEC v. Sloan*<sup>214</sup> the Court held that the SEC's power "summarily to suspend trading in any security . . . for a period not exceeding ten days" under section 12(k) of the Exchange Act did not permit the SEC to tack suspension periods so as to suspend trading indefinitely. The Commission relied on the absence of contrary statutory language or legislative history, the necessity for tacking "to maintain orderly and fair capital markets,"<sup>215</sup> the Commission's long-standing interpretation of the statute being "entitled to great deference,"<sup>216</sup> and implied subsequent congressional approval of tacking.<sup>217</sup> These arguments, all of which could be made for ancillary relief, were rejected. The Court concluded that "the Commission has not made a very persuasive showing that other remedies are ineffective,"<sup>218</sup> that Congress intended, by limiting summary suspensions to ten days, to balance the public interest against "the burden imposed on private parties,"<sup>219</sup> and even long-standing administrative interpretation cannot "overcome the clear contrary indications of the statute itself"<sup>220</sup> or the absence of clear congressional approval of tacking.<sup>221</sup> Finally, the Court noted that the power to suspend trading was "awesome" and that a "clear mandate from Congress . . . is necessary to confer this power."<sup>222</sup>

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213. 446 U.S. at 701.

214. 436 U.S. 103 (1978).

215. *Id.* at 115 (quoting from the Brief for the SEC at 37). The Commission argued that its other powers were "simply insufficient to accomplish its purposes" because injunctions and temporary restraining orders "take time and evidence to obtain and because they can be obtained only against wrongdoers and not necessarily as a stopgap measure in order to suspend trading simply until more information can be disseminated into the marketplace." *Id.* The SEC's tacking of 10-day suspension periods in the stock of Canadian Javelin, Ltd. had resulted in suspension of trading for over a year. *Id.* at 106.

216. *Id.* at 117.

217. *Id.* at 119-20.

218. *Id.* at 115. The Court noted that the Commission can move, and indeed in the case of CJL had moved, quickly to obtain a temporary restraining order or injunction and that the SEC can "simply reveal to the investing public . . . the reasons which it thought justified the initial summary suspension and then let the investors make their own judgments." *Id.* at 115-16.

219. *Id.* at 115.

220. *Id.* at 117.

221. *Id.* at 120-22.

222. *Id.* at 112.



These cases do not involve ancillary relief. Indeed, a principal objection in *Sloan* was to the SEC's failure to seek relief in court, an objection inapplicable to ancillary relief. But *Aaron* and *Sloan* do show the Court's reluctance to expand the SEC's enforcement power, especially when the power asserted is "awesome." At least some ancillary relief, such as the restructuring of corporate boards, is arguably more awesome than the actions of the SEC rejected in *Sloan*. *Sloan* and *Aaron* also show the Court's reluctance to infer congressional approval of past agency action and demonstrate some broader trends in the Supreme Court that were previously noted: statutory interpretation stressing literal statutory language rather than public policy or deference to agency interpretation, and a general hostility toward government regulation.<sup>223</sup> Those recent decisions in which the Court has not narrowed the scope of the securities laws offer no support for ancillary relief.<sup>224</sup> Rather, recent securities cases as a whole exemplify the judi-

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223. See *supra* notes 92-93, 98, 100, 104 and accompanying text.

224. In *United States v. Naftalin*, 441 U.S. 768 (1979), the Court held that section 17(a)(1) of the 1933 Act prohibits fraud against brokers as well as investors. The case demonstrates that just as the Court will not disregard statutory language and legislative history in order to expand the scope of the securities laws, neither will it disregard them in order to contract that scope. In *Steadman v. SEC*, 450 U.S. 91 (1981), the Court held that the SEC properly used the preponderance of the evidence standard of proof, rather than the clear and convincing standard, in an administrative proceeding to determine whether the defendant had violated the antifraud provisions of the securities laws. The Court relied primarily on the language and legislative history of the Administrative Procedure Act. *Rubin v. United States*, 449 U.S. 424 (1981), merely confirmed the holding of several lower courts on a minor point—a pledge of a security constitutes a sale for purposes of section 17(a) of the 1933 Act.

*Chiarella v. United States*, 445 U.S. 222 (1980), did confirm in dictum that rule 10b-5 bars insider trading on material nonpublic information. On that point it merely followed a rule well established in the lower courts. The case is more notable for restricting 10b-5 by ruling that it imposes no duty to disclose absent "a relationship of trust and confidence." *Id.* at 230.

In *Herman & MacLean v. Huddleston*, 103 S. Ct. 683 (1983), the Court held that a 10b-5 action is not precluded merely because the alleged violation might under other circumstances give rise to an action under section 11 of the 1933 Act. To some extent the decision undercuts the *expressio unius* reasoning the Court has used elsewhere. *Huddleston* is distinguishable from ancillary relief cases, though, in that it involved not the existence of an implied remedy but the scope of a well recognized remedy. Also, the arguments against certain ancillary remedies involve much more than the *expressio unius* reasoning rejected in *Huddleston*.

*Parklane Hosiery Co. v. Shore*, 439 U.S. 322 (1979), held that a party found at trial in an SEC injunctive action to have violated the securities laws may be collaterally estopped from relitigating the same issues of fact in subsequent action by a different plaintiff. The Court's entire discussion concerned the wisdom and constitutionality of permitting the offensive use of collateral estoppel. Nothing in the opinion is relevant to ancillary relief in the securities laws.

cial trend which favors deregulation by narrowing the scope of regulatory statutes.<sup>225</sup> While this trend does not necessarily dispose of the issue of ancillary relief, it does suggest an attitude potentially hostile to broad implied relief.

## C. THE FEDERAL SECURITIES LAWS AND CORPORATE GOVERNANCE

### 1. *Federalism and Santa Fe*

In addition to weighing the role of state law in deciding whether to infer a private damage action,<sup>226</sup> the Supreme Court has recognized that Congress intended the federal securities laws to occupy only a small part of the law governing corporations; the rest of the field was deliberately left to state control.<sup>227</sup> Thus federal courts must consider the relationship between federal and state law not only in molding federal common law but in determining congressional intent as to the relative scope of the federal securities laws and state corporation laws.

In *Santa Fe Industries, Inc. v. Green*<sup>228</sup> the Court held that a rule 10b-5 claim must allege deception or manipulation. The Court stressed that the plaintiff had alleged unfairness, not non-disclosure, and that the securities laws are concerned primarily with disclosure.<sup>229</sup> In deciding whether Congress intended to create a federal cause of action, the Court also considered whether the cause of action is traditionally governed by state law:

[T]his extension of the federal securities laws would overlap and quite possibly interfere with state corporate law . . . . Absent a clear indication of congressional intent, we are reluctant to federalize the substantial portion of the law of corporations that deals with transactions in securities, particularly where established state policies of corporate regulation would be overridden. As the Court stated in *Cort v. Ash*, supra: 'Corporations are creatures of state law, and investors commit their funds to corporate directors on the understanding that, except

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225. See Note, *supra* note 90, at 910-12.

226. The fourth factor listed in *Cort v. Ash* for deciding whether to imply a remedy is whether the cause of action is "one traditionally relegated to state law, in an area basically the concern of the States." 422 U.S. at 78.

227. See *infra* notes 230-33 and accompanying text.

228. 430 U.S. 462 (1977).

229. [A] private cause of action . . . should not be implied where it is "unnecessary to ensure the fulfillment of Congress' purposes." . . . [T]he Court repeatedly has described the "fundamental purpose" of the [Exchange] Act as implementing a "philosophy of full disclosure;" once full and fair disclosure has occurred, the fairness of the terms of the transaction is at most a tangential concern of the statute . . . .

*Id.* at 477-78.

where federal law *expressly* requires certain responsibilities of directors with respect to stockholders, state law will govern the internal affairs of the corporation.<sup>230</sup>

In other cases, too, the Court has relegated plaintiffs to state law rather than stretch federal law to cover the defendant's behavior.<sup>231</sup> *Burks v. Lasker*<sup>232</sup> held that whether directors of an investment company could terminate a derivative suit depended initially on state rather than federal law. The issues in *Burks* are very different from those in *Santa Fe* and

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230. *Id.* at 479 (emphasis added) (citation omitted). *Accord* Kaminsky v. Abrams, 281 F. Supp. 501, 504-05 (S.D.N.Y. 1968):

Federal securities legislation supersedes state corporate law remedies only to the extent of any direct conflict between the two, . . . and unless a matter is clearly covered exclusively by federal statute, it is deemed to be subject to state law. If Congress had intended to preempt the entire field, "so revolutionary a federal intervention," Loss says, "would presumably have been clearly expressed."

*Id.* (citing 2 L. Loss, *supra* note 57, at 903). *But cf.* Cort v. Ash, 422 U.S. 66, 85 (1975) (distinguishing *J.I. Case Co. v. Borak*, 377 U.S. 426 (1964)) ("In *Borak*, the statute involved [§ 14(a) of the Exchange Act] was clearly an intrusion of federal law into the internal affairs of corporations; to the extent that state law differed or impeded suit, the congressional intent could be compromised in state-created causes of action.").

Does either rationale for *Santa Fe* apply to SEC suits? Although the Court refers to implication of private actions in connection with the requirement of manipulation or deception, *see supra* note 229, the remainder of the discussion there and of federalism seems to apply equally to SEC suits. Application of *Santa Fe* is consistent with the intent of Congress as to the continuing role of state law. *See supra* notes 188-91 and accompanying text. Although no federal court has directly addressed the issue, *Santa Fe* has been cited with approval in SEC suits. *See* SEC v. Park Lane Hosiery, 558 F.2d 1083, 1088 (2d Cir. 1977); SEC v. Penn Central Co., 450 F. Supp. 908, 915 (E.D. Pa. 1978). *See also* Chiarella v. United States, 445 U.S. 222, 232 (1980) (criminal case). Accordingly, there is good reason to believe that *Santa Fe* does apply to SEC suits, and very little reason to believe otherwise.

231. *See* Piper v. Chris-Craft Indus., Inc., 430 U.S. 1 (1977); Cort v. Ash, 422 U.S. 66, 78 (1975).

*Edgar v. MITE Corp.*, 102 S. Ct. 2629 (1982), is not to the contrary. In *Edgar* the Court struck down the Illinois Business Take-Over Act as violating the Commerce Clause. In so doing, the Court rejected the claim that the Illinois Act merely regulated internal corporate affairs because "tender offers . . . do not themselves implicate the internal affairs of the target company." *Id.* at 2643. The state's power to regulate internal affairs was not challenged. Even the part of Justice White's opinion on preemption of the Illinois Act by the Williams Act, which was joined by only a minority of the Court, addresses an issue very different from *Santa Fe*. In *Edgar* the question was whether the Illinois Act frustrated the purposes of the federal securities laws; in *Santa Fe* the question was whether to interpret the federal securities laws so as to overlap or interfere with state law. Moreover, the Williams Act, in addition to requiring disclosure, reflects even-handed congressional intent regarding tender offers between bidders and target managements. In *Santa Fe*, by contrast, the Court noted that with respect to section 10(b) of the 1934 Act, disclosure was Congress's primary concern. 430 U.S. at 477-78.

232. 441 U.S. 471, 477-80 (1979).

from the question of ancillary relief, but the case further demonstrates the Court's regard for federalism in the securities laws.<sup>233</sup> Indeed, *Santa Fe* is but part of a growing concern for federalism that has affected both the Court's decisions in many areas, including the scope of federal common law,<sup>234</sup> and the programs of the political branches of the federal government.<sup>235</sup> Concern for federalism should be especially keen in the securities field because it arises not only from a general solicitude for state interests in our federal system but also from clear statements by Congress assigning certain areas of corporation law to the states.<sup>236</sup>

Clearly *Santa Fe* does not bar all interpretations of the federal securities laws that would differ from state law. Otherwise, the federal securities laws would merely replicate state law. Congress clearly intended that the federal securities laws correct many shortcomings in the state regulation of securities.<sup>237</sup> Nevertheless, *Santa Fe* is not limited to direct conflicts

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233. In *Santa Fe* the issue was the scope of federal law, rule 10b-5; state law became an issue only for the purpose of determining whether 10b-5 should be interpreted so as not to interfere with state law. In *Burks* the question was whether federal or state law should decide whether directors can terminate a derivative suit. The Court held that state law would govern "to the extent such law is consistent with the policies of" the Investment Company and Advisers Acts. 441 U.S. at 486. Although the contexts of the two cases are very different, *Burks* "is certainly consistent with the teaching of *Santa Fe* . . . and *Cort v. Ash* to the effect that the federal securities laws cannot be used as a backdoor approach to the federal chartering of corporations." Hazen, *The Supreme Court and the Securities Laws: Has the Pendulum Slowed?*, 30 EMORY L.J. 5, 29-30 (1981).

234. See *supra* note 100.

235. In his inaugural address President Reagan announced that turning back more functions to the states would be part of his legislative program. Smith, *Reversing the Liberalism of the New Deal*, N.Y. Times, Jan. 21, 1981, at B2. The "new federalism" phenomenon antedates the inauguration of President Reagan, however. See M. REAGAN & J. SANZONE, *THE NEW FEDERALISM* (2d ed. 1981).

236. See *supra* notes 210-13 and accompanying text.

237. For example, an injunction against violations of the securities laws could not be attacked for interfering with state law even in the rare case of clear conflict. The supremacy clause of the Constitution, art. VI, cl. 2, makes federal law the supreme law of the land. The question addressed by *Burks* and *Santa Fe*, however, is whether Congress has chosen to exercise its legislative power, or whether the federal courts should exercise their common-law-making power, to override state law. Not every difference between state and federal law makes the former inconsistent with the latter. *Burks v. Lasker*, 441 U.S. at 479-80.

Since the Court's concern for federalism springs largely from Congress's intent, it does not contradict the principle that federal law determines the remedies for violations of federal law. It is conceded that federal law determines the availability of ancillary relief. *J.I. Case Co. v. Borak*, 377 U.S. 426, 433-34 (1964); *Sola Elec. Co. v. Jefferson Elec. Co.*, 317 U.S. 173, 176 (1942). Rather the

with state law. In *Santa Fe* itself, the Court feared that interpreting rule 10b-5 to prohibit breaches of fiduciary duty or unfair transactions would "quite possibly interfere with state corporate law" although no state law even implicitly sanctioned such actions.<sup>238</sup> The Court has yet to draw lines here, but *Santa Fe* and *Burks* show that the Court is especially sensitive to intrusion on state control of corporate governance insofar as both cases involved questions of the duties of directors.<sup>239</sup> This sensitivity may be significant to ancillary relief affecting corporate governance.<sup>240</sup>

## 2. *The Purposes of the Securities Laws, the Scope of Disclosure, and Corporate Governance*

The SEC defends ancillary relief as necessary to effectuate the purposes of the securities laws by deterring violations and insuring future compliance.<sup>241</sup> This argument raises many questions about the purposes of the securities laws, especially as to ancillary remedies affecting corporate governance. Similar questions have arisen elsewhere in the securities laws. These questions may illuminate the issue of the propriety of ancillary relief.

One set of debates concerns the role of disclosure. The SEC and critics have disagreed on whether the Commission may compel disclosures reflecting on the integrity of manage-

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issue is, as in *Santa Fe*, whether in fashioning federal common law the courts should avoid interfering with state law.

238. Indeed, shortly after the decision in *Santa Fe*, the Delaware Supreme Court condemned the same kind of corporate freezeout of minority shareholders that the plaintiff had attacked in *Santa Fe*. See *Singer v. Magnavox Co.*, 380 A.2d 969 (Del. 1977).

239. *Santa Fe* refers to the "responsibilities of directors" and "the internal affairs of the corporation." 430 U.S. at 479.

240. See *infra* notes 313-22 and accompanying text.

241. Brief for SEC, *Amicus Curiae*, *General Steel Indus., Inc. v. Walco Corp.*, No. 81-2345 (8th Cir. 1981), reprinted in *Legal Times of Washington*, Jan. 4, 1982, at 18 ("deter violations," "afford shareholders adequate protection," and "effectuate Congress' purpose"); Brief for Appellee at 31, *SEC v. Western Geothermal & Power Corp.*, No. 79-3422 (1st Cir. 1979) ("preventing future violations"); Brief for Appellee at 25, *SEC v. Beisinger Indus. Corp.*, 552 F.2d 15 (1st Cir. 1977) ("to effectuate the purposes . . . and to provide effective enforcement"); 42 SEC ANN. REP. 108 (1976) ("to protect the public by deterring such conduct by others"). See Levine & Herlihy, *SEC Enforcement Actions*, 10 REV. SEC. REG. 951, 953 (1977) ("to restore accountability for wrongful conduct, to enhance the independent character of boards of directors, and to assure that recordkeeping and disclosure systems are adequate," the authors were officers in the SEC's Division of Enforcement); *SEC v. Mattel, Inc.*, 4 S.E.C. Doc. 724 [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,754 (D.D.C. 1974) ("to avoid a repetition of the alleged violations").

ment, especially disclosure of illegal activities, where the disclosures do not meet the financial materiality test.<sup>242</sup> Another question concerns disclosure intended to enable investors to assert rights under state law.<sup>243</sup> Some courts have required disclosure to shareholders about a transaction, even though the transaction is not submitted to shareholder vote but is approved by an interested board, if disclosure would have enabled shareholders to enjoin the transaction in state court.<sup>244</sup> A related controversy concerns the Commission's efforts under rule 13e-3 to require disclosure of management's opinion of the fairness of going private transactions to minority shareholders.<sup>245</sup> The Commission long ago conceded that disclosure

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242. The Commission argues that the integrity of management is always material to investors. See authorities cited in Branch & Rubright, *Integrity of Management Disclosures Under the Federal Securities Laws*, 37 BUS. LAW. 1447, 1447 n.2 (1982). The critics, who have received some support from the courts recently, see *Gaines v. Haughton*, 645 F.2d 761 (9th Cir. 1981), *cert. denied*, 102 S. Ct. 1006 (1982); Branch & Rubright, *supra*, at 1468-76, argue that, based on the legislative history and empirical studies of investor behavior, such disclosures are not material, except perhaps where they involve self-dealing by insiders or pending legal proceedings. See Branch & Rubright, *supra*, at 1479-85; Coffee, *Beyond the Shut-Eyed Sentry: Toward a Theoretical View of Corporate Misconduct and an Effective Legal Response*, 63 VA. L. REV. 1099, 1246-47 (1977); Kripke, *supra* note 158, at 188.

243. This is one possible basis for defending the Commission's rule 13e-3. See *infra* note 245.

244. See *Goldberg v. Meridor*, 567 F.2d 209 (2d Cir. 1977) (sale of stock by subsidiary to parent on terms allegedly unfair to minority shareholders of the subsidiary), *cert. denied*, 434 U.S. 1069 (1978). The problem also arises when minority shareholders are unable to block shareholder approval of a transaction because of the vote of an interested majority. See *Healey v. Catalyst Recovery, Inc.*, 616 F.2d 641 (3d Cir. 1980) (freezeout merger of a single minority shareholder). The author agrees with those who deny that this is a proper use of disclosure. First, disclosure should facilitate investment or proxy decisions, not litigation decisions. *Id.* at 651 (Aldisert, J., dissenting). Moreover, although plaintiffs argue that such disclosure supports state law, in practice it is much more likely to interfere with state law. *Id.* See also R. JENNINGS & H. MARSH, *SECURITIES REGULATION: CASES AND MATERIALS* 952 (5th ed. 1982) (criticizing *Goldberg* and *Healey*).

245. SEC Securities Act Release No. 16,075, [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,166 (1979). The SEC abandoned an earlier proposal that going private transactions be substantively fair. See SEC Securities Act Release No. 14,185, 13 S.E.C. Doc. 840 (1977). Broadly speaking, a going private transaction is any transaction which causes a public company to lose any substantial attribute of a public company, such as the delisting of stock on a stock exchange or the releasing from the statutory obligation to file periodic reports under section 12(g) of the 1934 Act. See Note, *Regulating Going Private Transactions: SEC Rule 13e-3*, 80 COLUM. L. REV. 782, 782 (1980) [hereinafter cited as Note, *Going Private*].

Critics charge that, although the SEC has packaged rule 13e-3 as a disclosure requirement, its true purpose and effect are to require fairness in going private transactions, and that this exceeds the Commission's powers. *Id.* at 795-97. Congress did not intend the statutory prohibition on fraud in section

should not be used primarily to affect corporate governance,<sup>246</sup>

13(e) to reach unfairness. See Sherrard, *Federal Judicial and Regulatory Responses to Santa Fe Industries, Inc. v. Green*, 35 WASH. & LEE L. REV. 695, 723-25 (1978); Note, *Going Private*, *supra*, at 790-92. The legislative history shows Congress revised the Williams Act to prohibit the SEC from getting involved in questions of the fairness of tender offers, and there is no evidence of any exception to this prohibition for going private transactions. See Note, *SEC Rulemaking Authority and the Protection of Investors: A Comment on the Proposed "Going Private" Rules*, 51 IND. L.J. 433, 443-46 (1976); Note, *Rule 13e-3 and the Going Private Dilemma: The SEC's Quest for a Substantive Fairness Doctrine*, 58 WASH. U.L. Q. 883, 909-10 (1980); Comment, *SEC Proposed "Going Private" Rule*, 4 DEL. J. CORP. L. 184, 206 (1978). Moreover, disclosures as to fairness intrude into state law because they give a shareholder a federal claim even if state law does not require fairness, and because a federal court may define fairness differently from a state court, in violation of the principles of federalism set forth in *Santa Fe*. See Note, *Going Private*, *supra*, at 797-98. One court has held that *Santa Fe* applied to section 13(e). See *Marshall v. AFW Fabric Corp.*, 441 F. Supp. 299, 300 (S.D.N.Y. 1977).

A similar dispute arose over the Commission's 1978 proposals to require the labeling of directors as management, affiliated non-management, or independent, and the disclosing of the extent to which the functions of any overview committee of the board differed from those listed by the SEC as usual for such committees. Proposed Rules Relating to Shareholder Communications, Shareholder Participation in the Corporate Electoral Process and Corporate Governance Generally, Items 6(a), (b), & (d), SEC Securities Exchange Act Release No. 14,970, [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,645 (July 18, 1978). The SEC ultimately withdrew these proposals after a storm of protest that they, too, were intended primarily to regulate substantive behavior by forcing corporations to adopt a particular mode of corporate governance, but the Commission never abandoned its position that the proposals required only disclosure and lay within its rule-making powers. The Commission insisted that it was making no value judgments about whether outside directors are preferable and that the proposals were not "designed primarily to influence corporate conduct rather than to provide useful information to shareholders" or to "prescribe or determine board composition or corporate governance mechanisms." SEC Securities Act Release No. 15,384, [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,766, at 81,087-88 (December 6, 1978). The Commission argued that any impact on corporate governance resulting from its proposals would be only an indirect result of disclosure, as Congress contemplated. *Id.* at 81,088. See *supra* note 171 and accompanying text.

246. In 1964 in *In re Franchard Corp.*, 42 S.E.C. 163, 176 (1964), the Commission conceded its lack of power to "define Federal standards of directors' responsibility in the ordinary operations of business enterprises." To impose such standards, said Chairman Cary, "would be basically incompatible with the philosophy and administration of the disclosure requirements of the Securities Act" and "would stretch disclosure beyond the limitations contemplated by the statutory scheme and necessitated by considerations of administrative practicality." *Id.* at 177-78. The Division of Corporation Finance argued that certain 1933 Act prospectuses, "by identifying the members of the board of directors, impliedly represented that they would provide oversight and direction to registrants' officers." *Id.* at 175-76. Thus the staff's proposal technically charged only a deficiency of disclosure. "The Commission apparently felt that a decision with respect to the sufficiency of disclosure would necessarily have involved them in a substantive determination of matters that lay within the province of state law." Sommer, *supra* note 24, at 123. See SEC Securities Act Release No. 1350 (1937) (SEC concedes it lacks power to pass on the fairness or

and the SEC's Advisory Committee on Corporate Disclosure recently adopted a similar position.<sup>247</sup>

The Commission's power to regulate proxy solicitations goes beyond requiring disclosure,<sup>248</sup> but even this power extends only to assuring the "fair corporate suffrage" that Congress intended;<sup>249</sup> it does not warrant further involvement in corporate governance. Indeed, even commentators who have noted the SEC's broader power to regulate proxies have conceded that this power does not extend to overruling other aspects of state corporation laws.<sup>250</sup>

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merits of any plan presented for shareholder vote); 1 L. LOSS, *supra* note 57, at 868-69.

247. Summarizing the relationship between disclosure and corporate governance, the Committee stated: "The Commission should not adopt disclosure requirements which have as their principal objective the regulation of corporate conduct . . . . If the Commission sees the need to directly regulate corporate conduct, it should request Congress to authorize it to do so . . . ." HOUSE COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE, 95TH CONG., 1ST SESS., REPORT OF THE ADVISORY COMMITTEE ON CORPORATE DISCLOSURE TO THE SECURITIES AND EXCHANGE COMMISSION 318-19 (Comm. Print 1979). See also SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS, 96TH CONG. 2D SESS., SEC STAFF REPORT ON CORPORATE ACCOUNTABILITY 750 (Comm. Print 1980). The SEC questioned whether the principle espoused by the Advisory Committee should be embodied in a statement of objectives by the Commission. It feared it might lead to "[d]ebate as to what was the Commission's primary, as distinct from secondary, objective in taking particular action." SEC Securities Act Release No. 5906 (Feb. 15, 1978), [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,505, at 80,048. It is not clear whether the SEC rejected the principle advanced by the Advisory Committee or merely the idea of announcing that principle in a Commission statement of objectives. See also Weiss & Schwartz, *supra* note 174, at 84 & n.93 ("The Commission would probably have to obtain new legislative authority in order to enforce . . . substantive rules governing the composition and organization of boards of directors.").

248. See SEC STAFF REPORT ON CORPORATE ACCOUNTABILITY, *supra* note 247, at A-42—A-44 and authorities cited therein. See also Caplin, *Proxies, Annual Meetings and Corporate Democracy: The Lawyer's Role*, 37 VA. L. REV. 653, 684-85 (1951). The SEC has rarely used this broader power. It is difficult to categorize many requirements of proxy rule 14a as disclosure requirements. For example, although rule 14a-8, requiring the inclusion in management's proxy statement of various types of shareholders' proposals, might not at first glance seem to be a disclosure requirement one ground on which the SEC and commentators have justified 14a-8 is that it is necessary in order to inform shareholders of proposals that may be brought before the meeting. See Schwartz & Weiss, *An Assessment of the SEC Shareholder Proposal Rule*, 65 GEO. L.J. 635, 639 (1977). Some others, such as the requirement of rule 14a-4(b)(1) that shareholders be given an opportunity to abstain on any question to be voted upon, are more difficult to categorize as disclosure requirements, but are still narrowly limited to the proxy area and do not otherwise affect corporate governance.

249. See *supra* note 176 and accompanying text.

250. See 2 L. LOSS, *supra* note 57, at 902-03 (SEC may not require inclusion of shareholder proposals on matters that are not appropriate for action under state law).



Disclosure issues, although not directly in issue in most ancillary relief cases, are nonetheless relevant to ancillary relief in several ways. First, in weighing the benefits of ancillary relief (in terms of deterring securities law violations by improving disclosure) against the detriments (such as interfering with state law or with shareholder democracy), it must be remembered that the scope of securities disclosure is not unlimited. Second, if the SEC cannot interfere with corporate governance through rules the "principal objective" of which is "the regulation of corporate conduct,"<sup>251</sup> a fortiori the Commission cannot regulate corporate governance more directly by the restructuring of corporate boards via ancillary relief.

Controversy has also raged over the SEC's use of its Rule of Practice 2(e)<sup>252</sup> to discipline professionals, especially attorneys, who engage in activities the SEC deems illegal or unethical. Although the Commission has occasionally supported rule 2(e) as promoting the purposes of the securities laws, its principal arguments have concerned its power to protect the integrity of its processes.<sup>253</sup> Thus the rule 2(e) debate is of little

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251. See *supra* note 247 and accompanying text.

252. 17 C.F.R. § 201.2(e) (1982).

253. Through rule 2(e), the Commission asserts the power to deny, temporarily or permanently, the privilege of appearing or practicing before it in any way to any person who is found by the Commission . . . to be lacking in character or integrity or to have engaged in unethical or improper professional conduct, or . . . to have willfully violated, or willfully aided and abetted the violation of the federal securities laws or rules.

*Id.* See *In re Carter & Johnson*, SEC Securities Exchange Act Release No. 17,597, [1981 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,149 (1981); *In re Keating, Muething & Klekamp*, SEC Securities Exchange Act Release No. 15,982, 17 S.E.C. Doc. 1149, 1164 (Chairman Williams, concurring). *Accord* *Touche Ross & Co. v. SEC*, 609 F.2d 570, 580-81 (2d Cir. 1979) (dealing with the application of rule 2(e) to accountants, though in dictum the court also approved its application to attorneys). It is sometimes argued that rule 2(e) is valid because it promotes the purposes of the securities laws by ensuring that professionals, on whom so much of securities compliance depends, perform with diligence and competence. *Id.* at 580-81. This argument seems generally to be secondary, however.

The author tends to agree with critics who deny that the SEC can properly apply rule 2(e) to lawyers. See, e.g., *In re Keating, Muething & Klekamp*, SEC Securities Exchange Act Release No. 15,982, 17 S.E.C. Doc. 1149, 1157 (1979) (Commissioner Karmel, dissenting) (SEC's program is in aid of its prosecutorial function and thus rule 2(e) is an invalid exercise of its power); Marsh, *Rule 2(e) Proceedings*, 35 BUS. LAW. 987, 1005, 1010-15 (1980) (rule 2(e) violates statutory grant to district courts of exclusive jurisdiction over violations of the securities laws and may violate the constitutional right to due process); Miller, *The Distortion and Misuse of Rule 2(e)*, 7 SEC. REG. L.J. 54, 59 n.13 (1979) (where Congress intended agencies to have general rule-making and disciplinary authority, it has been explicit); Note, *SEC Disciplinary Proceedings Against Attorneys Under Rule 2(e)*, 79 MICH. L. REV. 1270, 1275-77, 1285 (1981)

relevance to ancillary relief and the role of the SEC in corporate governance.

On occasion the Commission has considered regulating corporate governance directly. In 1973 the SEC announced a project to set standards for directors of public companies.<sup>254</sup> The project was abandoned the following year.<sup>255</sup> In 1978 the Commission commenced an inquiry on whether it could require public companies to have audit committees composed of outside directors. The Commission never adopted such a rule, however.<sup>256</sup> Before the proceeding was abandoned, Harvey L. Pitt, the SEC's General Counsel, issued an opinion supporting the Commission's power to adopt an audit committee rule. He found this authority in the SEC's powers to require certification of financial statements by an independent accountant, to define certain accounting terms, and to implement the requirement of the Foreign Corrupt Practices Act that public companies maintain adequate systems of internal accounting controls.<sup>257</sup>

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(noting lack of express authority to regulate attorneys as compared with express authority to regulate many others). Most of these criticisms have little bearing on corporate governance. Professor Kripke, however, has also argued that rule 2(e) interferes improperly with corporate governance. Kripke, *supra* note 158, at 201.

254. See Address by G. Bradford Cook, Southern Methodist University School of Business Administration (April 6, 1973), *reprinted in* [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 79,302 (discussing the responsibilities of the corporate director under federal securities laws).

255. The project was abandoned, ostensibly because of the difficulty of defining standards, but also perhaps because of doubts about the Commission's power to impose such standards. Compare Comments of Ray Garrett, Jr., Annual Corporate Counsel Institute, at 4-5 (Oct. 3, 1974), *discussed in* [1974] SEC. REG. & L. REP. (BNA) No. 272, at A-11 (Oct. 9, 1974) (defending disclosure regulations), with Coffee, *supra* note 242, at 1248 (doubting Commission's authority).

256. Under pressure from the SEC, the New York Stock Exchange adopted a rule requiring listed companies to have audit committees, thereby diminishing the need for Commission action. See NEW YORK STOCK EXCHANGE, COMPANY MANUAL, at A-29; 2 N.Y.S.E. GUIDE (CCH) ¶ 2495H. Even public companies not listed on the NYSE usually now have audit committees. An SEC survey of companies subject to the proxy rules showed that nearly 80% of companies not on the NYSE had audit committees. SEC Securities Act Release No. 17,518, 21 S.E.C. Doc. 1551, 1567 (Feb. 5, 1981). See Letter from SEC Chairman Roderick M. Hills to Mr. William M. Batten, Chairman of the New York Stock Exchange (May 11, 1976), *reprinted in* [1976] SEC. REG. & L. REP. (BNA) No. 353 (Special Supp.), at 44-45 (May 19, 1976) (encouraging NYSE to require audit committees).

257. *Opinion of SEC General Counsel on the Commission's Authority to Require Public Companies to Establish Independent Audit Committees*, *reprinted in* [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,535, at 80,177-81 (March 2, 1978).

Even if Mr. Pitt's arguments were accepted,<sup>258</sup> however, they would not justify most ancillary relief affecting corporate governance. The proposed audit committee rule would have intruded less into corporate governance than ancillary relief often does. Through ancillary relief the Commission has often required not only an audit committee of outsiders but also an outside majority on the entire board, with the SEC in effect picking those outsiders. More important, Mr. Pitt's justifications apply to accounting matters and not to other interference in corporate governance. Even critics of the Commission's attempts to expand its regulation admit that it has broad untapped powers to regulate accounting and accountants,<sup>259</sup> powers that do not extend to corporate governance generally.

Because the courts have not resolved these many disputes over disclosure and SEC involvement in corporate governance, no firm conclusions can be drawn from them. Several points are worth noting, however. On occasion, notably in *Franchard*, the Commission has conceded its lack of authority to interfere in corporate governance.<sup>260</sup> Whenever the SEC has suggested direct regulation of, or disclosure rules affecting, corporate governance, commentators and the bar have questioned the Commission's authority. When faced with such criticism, the SEC has often retreated from its proposals. The Commission has also regularly disclaimed any intent to interfere in corporate governance through its proposals. These points provide no dispositive arguments against ancillary relief affecting corporate governance. They do, however, tend to support the conclusions about the SEC and corporate governance reached in the above analysis of the legislative history and of *Santa Fe*.

## V. ANCILLARY RELIEF IN SECURITIES LAW

What conclusions can be drawn about ancillary relief in securities law? This Part considers general approaches to ancillary relief, the propriety of specific remedies in contested cases, and finally, the significance of the defendant's consent.

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258. In particular, if outside members of an audit committee must be members of the board, an audit committee rule would also require a minimum number of outside directors, who would participate in all of the board's decisions. In light of Congress' emphasis on disclosure and opposition to direct Commission involvement in corporate governance, *see supra* notes 173-99 and accompanying text, it seems unlikely that Congress intended to sanction such a rule.

259. *See* H. KRIPKE, *supra* note 140, at 141-43.

260. *See supra* note 246.

## A. A GENERAL APPROACH TO ANCILLARY RELIEF

Although respectable arguments can be made for denying virtually any relief not expressly authorized by the securities laws, or for approving any relief subject only to trial court discretion, these arguments are ultimately unpersuasive. Instead, this Article proposes an analysis that considers each type of ancillary relief separately in light of relevant considerations.

1. *A Blanket Prohibition on Ancillary Relief?*

Should courts in securities cases deny all ancillary relief? Supreme Court discussion of the issue is limited to *Deckert*, but the facts there are distinguishable from most ancillary relief cases, and the Court's discussion of ancillary relief is dictum.<sup>261</sup> The legislative history of the securities laws reveals no congressional intent to authorize ancillary relief,<sup>262</sup> and the express provision for many ancillary remedies in other statutes, including some securities legislation, further belies any such intent.<sup>263</sup> Statements of the broad inherent remedial powers of equity are suspect as vague, subject to exceptions, and obsolete because of recent cases restricting statutory interpretation and federal common law.<sup>264</sup> Most cases approving ancillary relief in other areas of administrative law are distinguishable as involving differently worded statutes.<sup>265</sup>

While the foregoing factors weaken the case for ancillary relief, they establish no affirmative argument against it. Neither do recent Supreme Court cases compel prohibition of ancillary relief. Cases curtailing the securities laws and implied private actions involve issues quite different from ancillary relief.<sup>266</sup> While these cases, the restriction of federal common law, and the movement toward literalism in statutory interpretation evince some hostility to governmental regulation and judicial activism, they establish no complete bar on ancillary relief. The Court continues on occasion to interpret the securities laws broadly, to fashion federal common law, to go beyond statutory language in statutory interpretation, and even to approve implied private damage actions.<sup>267</sup> Lower courts

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261. See *supra* notes 50-52 and accompanying text.

262. See *supra* notes 169-99 and accompanying text.

263. See *supra* notes 161-67 and accompanying text.

264. See *supra* notes 78-106 and accompanying text.

265. See *supra* notes 62-63 and accompanying text.

266. See *supra* notes 107-48, 205-40 and accompanying text.

267. See *Pennhurst State School v. Halderman*, 451 U.S. 1, 18 (1981) (court must look to the "whole law, and to its object and policy"); *supra* notes 148 (re-

have approved a variety of ancillary remedies,<sup>268</sup> and the Supreme Court has refused on occasion to reject implied remedies long accepted by the lower courts.<sup>269</sup>

The absence of any reference to ancillary relief in the legislative history should not be fatal; nothing in that history expressly forbids ancillary relief, and the traditions of equity and precedents involving ancillary relief clearly support many ancillary remedies. Many members of Congress probably knew of equity's tradition of granting ancillary relief and may have intended to authorize remedies traditionally granted by equity which would further the purposes of the securities laws. Prohibiting ancillary relief would require courts to disregard the ability of many ancillary remedies to further these purposes. In sum, very little in law or public policy calls for a complete ban on ancillary relief.

## 2. *A Blanket Approval Subject to Judicial Discretion?*

Antipodal to a blanket prohibition on ancillary relief would be a blanket approval, subject only to the trial court's discretion to mold relief to the facts of each case. Under this approach the Supreme Court would at most list factors that the trial court should consider, and any ancillary remedy would be affirmed unless the trial court abused its discretion. Although commentators have expressed some qualms about ancillary relief, this is the approach which they have recommended<sup>270</sup> and which the courts have followed.<sup>271</sup> The position is beguiling—how can ancillary relief be inappropriate in a given case if a trial court has, after considering all relevant factors, approved

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cent Supreme Court cases inferring private remedies), 227 (recent Supreme Court decisions broadly interpreting the federal securities laws).

268. See cases cited *supra* notes 11-13, 16-22.

269. For example, the Court has explained its recognition of an implied damage action under rule 10b-5 as a mere acquiescence in the long-standing recognition of such an action by the lower federal courts. *Touche Ross & Co. v. Redington*, 442 U.S. 560, 577-78 n.19 (1979); *Cannon v. University of Chicago*, 441 U.S. 677, 692 n.13 (1979). See also *id.* at 692-93 n.13 (explaining recognition of implied causes of action under various sections of the Railway Labor Act).

270. See Farrand, *supra* note 4, at 1807-14; Comment, *Court Appointed Directors*, *supra* note 4, at 766-67; and Comment, *Equitable Remedies*, *supra* note 4, at 1214-16, all recommending that trial courts proceed cautiously in ancillary relief cases and listing factors courts should consider in exercising their discretion in such cases. See also Treadway, *supra* note 4, at 679 (recognizing problems with ancillary relief but making no recommendations to curb it except that the SEC should establish rules governing ancillary relief).

271. Although courts have occasionally rejected or counselled caution about ancillary relief, see *supra* note 10, they have generally approved such relief, see *supra* notes 11-49 and accompanying text.

the relief, which is not found on appeal to have been an abuse of discretion? Though beguiling, this approach should be rejected because the courts cannot handle the problems of ancillary relief<sup>272</sup> on a case-by-case basis. There are three principal reasons for this.

First, the Supreme Court and the courts of appeals cannot effectively control the district courts' discretion in ancillary relief. Even critics of the Supreme Court's recent decisions restricting the federal securities laws concede that the lower courts have often expanded these laws excessively.<sup>273</sup> The Court's rulings recognize that in some areas hard and fast rules, even if somewhat crude, are preferable to rules leaving the district courts broad discretion, because the Court cannot regularly monitor lower court rulings and prevent erosion of basic principles.<sup>274</sup> Effective appellate review is especially problematic in ancillary relief cases. The SEC, the plaintiff in most such cases, has considerable leverage over most defendants<sup>275</sup> and can often extract consent decrees, thereby avoiding appellate review. In addition, ancillary relief may harm persons, especially shareholders, who are not represented in court and cannot appeal, even in a contested case. Finally, in a contested case ancillary relief, especially relief affecting corporate governance, would have to be premised on a complicated trial record, which further complicates appellate review. The difficulties of appellate review are borne out by the infrequency of reversals of ancillary relief cases.<sup>276</sup> In addition, the Supreme Court can review such cases only rarely. To exercise any control at all, it must limit district court discretion.

One cannot meet these objections by assuming, in light of past behavior, that the Commission will restrain itself. In ancil-

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272. These problems include undue SEC interference in corporate governance, infringement of shareholder suffrage, state control of corporate governance, congressional control of enforcement activities of administrative agencies, and the granting of remedies that do not further the purposes of the securities laws. See *infra* notes 312-22, 339-43, 361-64 and accompanying text.

273. See Frankel, *supra* note 112, at 582-83 (although the Supreme Court has gone too far in limiting implied private damage actions, some restrictions were necessary). Some attribute the Court's restriction of implied damage actions to the lower courts' having gotten "out of hand." Note, *supra* note 93, at 370.

274. See *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 755 (1975) (declining to leave the purchaser-seller rule of rule 10b-5 "open to endless case-by-case erosion").

275. See *infra* notes 372-76 and accompanying text.

276. The difficulty is compounded by the holding of some courts that appellants must meet a "heavy burden" of proving that the district court abused its discretion. See *SEC v. Koenig*, 469 F.2d 198, 202 (2d Cir. 1972).

lary relief, as in many other areas, the SEC has aggressively pushed its powers as far as the courts have allowed.<sup>277</sup> Especially in the realm of corporate governance, the SEC has ignored the weakness of its claims of jurisdiction and has acted so aggressively as to persuade some commentators that it wants to preempt the state corporate laws.<sup>278</sup>

A case-by-case approach also creates undue uncertainty among defendants as to what relief can be extracted from them. Where a trial court has vast, essentially unreviewable discretion as to remedies, defendants feel even more than the usual compulsion to settle rather than to risk the unknown.

Finally, and most important, respect for congressional intent may render certain ancillary remedies inappropriate either in certain definable circumstances or under any circumstances. Despite the flexibility of equity, it is hardly unprecedented to limit the discretion of the chancellor. The Supreme Court has not only demanded certain conditions on the grant of an injunction<sup>279</sup> but has also curbed the implication of statutory remedies, once thought to be limited only by the discretion of equity.<sup>280</sup>

One could argue that Congress knew of equity's practice of granting ancillary relief and therefore intended, by empowering the courts to grant injunctions, to permit any remedy a court

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277. See Freedman & Sporkin, *The Securities and Exchange Commission's Enforcement Program: A Debate on The Enforcement Process*, 38 WASH. & LEE L. REV. 781, 781 (1981) (comments of Professor Freedman) ("[T]he enforcement work of the Commission, at best, reflects an over-zealous insensitivity to individual liberties and the values of a free society; and, at worst, a deliberate pattern of serious and inexcusable violations of fundamental rights and elementary notions of fairness."). In particular, Professor Freedman attacks the Commission for its use of rule 2(e) to force lawyers to enforce the securities laws, for abusing "its power of obtaining publicity at pretrial stages to impose very severe punishment without due process," and for abusing consent decrees. *Id.* at 782-85. See also H. KRIPKE, *supra* note 140, at 47-51 (SEC abuse of injunctive proceedings). To some extent, abuse of enforcement proceedings may flow from the unwillingness or inability of the Commission to control the enforcement staff. See Coffee, *supra* note 242, at 1248 n.531. But the Commission itself has often pushed the securities laws to their limits and beyond. This is reflected both in the large number of Supreme Court cases the Commission has lost lately, see *supra* notes 207-40 and accompanying text, and in the many current controversies in which the Commission has been criticized for exceeding its jurisdiction, see *supra* notes 242-60 and accompanying text.

278. Rosenfeld, *Corporate Governance*, 77 SEC. REG. L.J. 171, 172 (1979). See Kripke, *supra* note 158, 172-73, 182.

279. See *supra* note 86 and accompanying text. See generally *supra* notes 81-87 and accompanying text.

280. See *Porter v. Warner Holding Co.*, 328 U.S. 395, 398 (1946); *Deckert v. Independence Shares Corp.*, 311 U.S. 282, 288 (1940).

deems appropriate.<sup>281</sup> There are several problems with this argument, however. First, there was no tradition of ancillary relief in administrative law in 1933-34 for the obvious reason that federal administrative law did not exist to any significant degree at that time. Nor was there precedent anywhere in equity for certain ancillary remedies, such as the restructuring of corporate boards. Second, if Congress was relying on an inherent judicial power to fashion ancillary remedies, presumably it would not have bothered to provide expressly, as it did in the 1934 Act and in later securities and other legislation, for certain ancillary remedies.<sup>282</sup> At least Congress could have provided, as it did elsewhere,<sup>283</sup> for the issuance of an injunction "or other order." Third, even if Congress did intend to permit the judiciary to fashion ancillary relief, there is no evidence that it intended to leave ancillary relief solely to the discretion of the district courts. It is entirely appropriate for appellate courts to provide standards for ancillary relief. The results of the case-by-case approach, which now prevails, are that the district courts are assuming the essentially legislative function of defining remedies for statutory violations, often disregarding the purposes of the securities laws.

### 3. *Toward a General Approach to Ancillary Relief*

If neither a blanket prohibition nor a blanket approval of ancillary relief is appropriate, what is the correct approach? The answer lies in evaluating ancillary remedies in the light of the purposes of the securities laws as revealed by their express language and legislative history, the traditions of equity, and the proper role of the federal courts in fashioning implied statutory remedies. Since these factors weigh differently on different remedies, the propriety of each type of ancillary relief must be considered separately. Nonetheless, some general principles can be established.

In recent years the Supreme Court has fundamentally redefined the roles of Congress and the federal courts in fashioning remedies under federal statutes. Formerly, the federal

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281. See *Mitchell v. Robert DeMario Jewelry, Inc.*, 361 U.S. 288, 291-92 (1960) ("When Congress entrusts to an equity court the enforcement of prohibitions contained in a regulatory enactment, it must be taken to have acted cognizant of the historic power of equity to provide complete relief in light of the statutory purposes."). Accord *Chris-Craft Indus., Inc. v. Piper Aircraft Corp.*, 480 F.2d 341, 390 (2d Cir.), cert. denied, 414 U.S. 910 (1973).

282. See *supra* notes 161-65 and accompanying text.

283. See *supra* notes 62-63, 162 and accompanying text.



courts readily implied such remedies as matters of federal common law whenever they thought it desirable public policy.<sup>284</sup> The Court now views the implication of remedies more as a matter of statutory interpretation because it sees Congress as the preferable body under our constitutional scheme to specify statutory remedies.<sup>285</sup> Moreover, the Court now balks at deciding for itself what remedies will best serve public policy. In particular, if a statute reveals conflicting purposes, the Court will hesitate to choose between them; rather it will defer to the literal statutory language. If in such a case Congress has not specified a remedy, the Court will hesitate to create one.<sup>286</sup>

One cannot be sure how these general trends will affect ancillary equitable relief in administrative law because the Court has not recently addressed the issue. These trends have not led to absolute rules in other areas,<sup>287</sup> however, and ancillary relief differs from other areas where these trends have appeared. So the Court will probably not bar ancillary relief completely, but it will undoubtedly be more restrictive than it has been in the past.

This restrictive attitude is supported by the lack of any reference to ancillary relief in the legislative history of the securities laws. Amendment of the securities laws has been held not to constitute congressional approval of all prior judicial holdings and practices,<sup>288</sup> and should not be so held as to ancillary relief.<sup>289</sup> Courts may infer congressional approval of remedies

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284. See *supra* note 112 and accompanying text.

285. See *supra* notes 117-20, 129, 144-47 and accompanying text.

286. See *Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630 (1981). The Court described the competing arguments as to whether there should be a right to contribution among antitrust defendants and then concluded that "[t]he range of factors to be weighed . . . demonstrates the inappropriateness of judicial resolution of this complex issue." *Id.* at 646. See also *supra* notes 117-20, 128 and accompanying text. Indeed, the SEC has agreed in principle that where the intent of Congress is ambiguous, the SEC should seek clarification from Congress. See *Ruder, Pitfalls in the Development of a Federal Law of Corporations by Implication Through Rule 10b-5*, 59 Nw. U. L. Rev. 185, 189-90 (1964) (quoting a letter from J. Sinclair Armstrong, then chairman of the SEC, SEC Securities Act Release No. 3762, at 5 (1957)).

287. Thus, for example, the Court continues to weigh legislative purpose when interpreting statutes, see *supra* note 102, and to create implied statutory remedies in certain cases, see *supra* note 148.

288. *Aaron v. SEC*, 446 U.S. 680, 694 n.11 (1980) (discussed *supra* text accompanying notes 235-36); *SEC v. Sloan*, 436 U.S. 103, 119-22 (1978) (discussed *supra* text accompanying notes 214-22).

289. There is no evidence of "general congressional awareness" of the practice of ancillary relief, see *SEC v. Sloan*, 436 U.S. 103, 121 (1978), and Congress has not "focused on issues . . . directly related to" ancillary relief, *id.* at 120. As to the more exotic remedies such as those affecting corporate governance,

traditional to equity, but not of remedies that are unknown to equity and have not been awarded in other areas of administrative law. The argument is strong in the latter case that Congress did not intend to authorize such remedies either when it originally adopted the securities laws or when it amended them. The absence of a remedy through the long history of equity, especially at the time the legislation was enacted, also counsels caution against finding that remedy important to the fulfillment of a statutory purpose.<sup>290</sup> For the same reasons, courts should hesitate to abandon conditions equity has traditionally imposed on the grant of an ancillary remedy.<sup>291</sup>

While the importance of each type of ancillary relief to the securities laws may be relevant, the SEC's claim that certain remedies are necessary is by no means conclusive. In *SEC v. Sloan*<sup>292</sup> the Supreme Court deemed "unpersuasive" the SEC's argument that effective enforcement required that it be able to tack ten-day periods of suspension of trading in particular securities. Indeed, if the statutory scheme and legislative history clearly negate a remedy, *Sloan* states that a court may not fashion the remedy no matter how desirable: "the proper source of that power is Congress."<sup>293</sup>

Where the statutory language and legislative history do not bar a remedy, as they did in *Sloan*, the importance of ancillary relief to effective enforcement should be weighed. This importance depends in part on the potency of the express remedies available. The SEC first sought ancillary relief because it felt that an injunction against future violations was a mere slap on the wrist, insufficient to deter the defendant or others from future violations.<sup>294</sup> In imposing stiff conditions on the granting of injunctions, however, courts have recently noted that an in-

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moreover, there has not been established any judicially accepted position in which Congress might acquiesce.

290. "[T]he initial focus must be on the state of the law at the time the legislation was enacted." *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 102 S. Ct. 1825 (1982). "It is always appropriate to assume that our elected representatives, like other citizens, know the law . . ." *Cannon v. University of Chicago*, 441 U.S. 677, 696-97 (1979). *Accord Merrill Lynch*, 102 S. Ct. at 1839. The principle also applies to re-enactments of a statute. *Id.* at 1841 n.66 and authorities cited therein.

291. See *supra* notes 81-89 and accompanying text.

292. 436 U.S. 103 (1978). See *supra* notes 214-22 and accompanying text.

293. 436 U.S. at 115-17. *Sloan* is discussed in greater detail at *supra* notes 214-22 and accompanying text. See also *Blau v. Lehman*, 368 U.S. 403, 411-13 (1962) (refusing to expand section 16(b) of the Exchange Act despite possibly "persuasive policy arguments that the Act should be broadened").

294. See *supra* note 25.

junction is strong medicine; it not only threatens criminal contempt for future violations but it also triggers many disabilities under the securities laws.<sup>295</sup> The SEC has often argued that the egregiousness of defendants' violations shows that they cannot be trusted, even under the burden of an injunction, to obey the law, but the SEC has never empirically demonstrated, or even attempted to demonstrate, that securities law violators, even egregious violators, are likely to disobey an injunction.<sup>296</sup> It is one thing to violate the securities laws; it is quite another to violate them again after having been caught the first time and subjected to an injunction. Although ancillary remedies may be necessary for effective enforcement in some cases, the courts should reject any general claim by the Commission that an injunction is insufficient. The Commission should be required to prove the claim in each case separately.

#### B. ANCILLARY RELIEF IN CONTESTED CASES

##### 1. *Remedies to Rectify Past Violations—Disgorgement, Restitution, Rescission, Sterilization of Voting Rights, Etc.*

The SEC has often stressed that it is not a collection agency for defrauded investors.<sup>297</sup> Since the legislative history expresses no support for disgorgement, restitution, or rescission, can these remedies be justified?

Disgorgement, restitution and rescission are long-eslab-

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295. See *SEC v. Commonwealth Chem. Secs., Inc.*, 574 F.2d 90, 99 (2d Cir. 1978); Note, *Injunctive Relief in SEC Civil Actions: The Scope of Judicial Discretion*, 10 COLUM. J.L. & SOC. PROBS. 328, 340-42 (1974). The SEC rarely seeks contempt. Coffee, *supra* note 77, at 453 n.185. Indeed, it has been suggested that the disabilities imposed on persons subject to injunctions under SEC rules violate the principle that injunctions should deter, not punish. Wax, *The Emerging SEC Injunction*, 17 N.Y.L.F. 785, 785 (1971).

296. Although a few ancillary relief cases have involved violations of prior decrees, the number is apparently small. See, e.g., *SEC v. Beisinger Indus. Corp.*, 552 F.2d 15, 19 (1st Cir. 1977); *SEC v. Heritage Trust Co.*, 402 F. Supp. 744, 753 (D. Ariz. 1975). Cf. Posner, *A Statistical Study of Antitrust Enforcement*, 13 J. LAW & ECON. 365, 385-87 (1970) (successful prosecutions for contempt for violating antitrust decrees are so rare as to raise questions whether they serve "much purpose, except in cases where the law is in doubt").

297. See 41 S.E.C. ANN. REP. 97-98 (1975) ("The SEC's primary function is . . . not to obtain damages for injured individuals."). See also Cary (former SEC Chairman), Book Review, 75 HARV. L. REV. 857, 860-61 (1962) (noting the need for efficient use of limited SEC manpower and monetary resources); Speech of SEC Commissioner Richard B. Smith at the Program of Continuing Legal Educ. of the California Bar, in Los Angeles (Jan. 12, 1968) (on file at the SEC library, Washington, D.C.) ("The Commission attempts to avoid being a collection agency for injured investors . . .").

lished remedies of equity.<sup>298</sup> They may also contribute significantly to effective enforcement of the securities laws. Many ways of violating those laws, especially insider trading, can produce handsome profits with little risk of being caught.<sup>299</sup> If the SEC can only enjoin insider trading, potential offenders will know that they can retain their unjust enrichment unless they are sued privately. In general, restitution and disgorgement do not intrude into any areas from which Congress intended to exclude the Commission.

Ancillary relief is unnecessary, however, to effective enforcement if relief can be obtained through a private action.<sup>300</sup> In many cases private relief will be available; the express provisions of the 1934 Act apparently permit an action for rescission or restitution by a defrauded buyer.<sup>301</sup> An SEC request for restitution or rescission implies that the identity of the persons defrauded is known. These persons presumably could sue privately for such relief. An SEC action for rescission and restitution might be more efficient than multiple private suits and might avoid the practical and procedural problems of a class action, but an SEC action hardly seems crucial to the enforcement of the securities laws. Such an action reduces the SEC to little more than a collection agency, contrary to the intentions of Congress. Accordingly, the SEC should be granted rescis-

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298. See D. DOBBS, HANDBOOK ON THE LAW OF REMEDIES 223-27 (disgorgement of unjust enrichment), 229-40 (history of restitution), 254-56 (rescission) (1973).

299. W. CARY & M. EISENBERG, CASES AND MATERIALS ON CORPORATIONS (5th ed. 1980) 728-29. Inside traders are subject to private suits under rule 10b-5. *Chiarella v. United States*, 445 U.S. 222, 226-30 (1980). Although the Court has recently hesitated to recognize new implied private rights of action, see *supra* notes 115-25 and accompanying text, it has not questioned the continuing availability of such an action under rule 10b-5. But the odds of detection are small, and some courts have impeded recovery even from one who is caught if, as is usually the case, the trading occurred on an impersonal exchange. *Fridrich v. Bradford*, 542 F.2d 307, 318-19 (6th Cir. 1976), *cert. denied*, 429 U.S. 1053 (1977) (apparently demanding proof of some privity or causation by plaintiff, proof that would be very difficult to show when defendant traded on an impersonal exchange). See also *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 754-55 (1975) (requiring that the plaintiff in a 10b-5 action be a purchaser or seller). *Blue Chip* generally prevents the issuer (or any of its shareholders by a derivative suit) from suing under 10b-5 for insider trading.

300. Ancillary relief in such a case also violates the maxim that equity should act only where there is no adequate remedy at law. *Ellsworth*, *supra* note 4, at 648. There is also some question whether an administrative agency is authorized to sue in what is essentially a private dispute. See *id.* at 649.

301. Section 29(b) of the Act, which declares void any contract violative of the Act, is very similar to section 215 of the Investment Advisors Act, which the Court in *Transamerica* held to authorize an action for rescission or restitution. See *supra* note 124.

sion or restitution only if a private action is impossible, perhaps because no private action is permitted for the violation in question. Disgorgement stands on a different footing if rescission and restitution are unavailable because the defrauded victims are unknown. The SEC should be able to seek disgorgement in such cases.<sup>302</sup> If private suits for restitution or rescission are pending, an SEC suit for the same relief or for disgorgement may be stayed until the private suits are resolved.<sup>303</sup>

Sterilization of voting rights for illegally acquired stock is another appropriate ancillary remedy. An injunction against future violations, without more, not only leaves defendants their ill-gotten gains but also permits them to add to those gains every time they vote their shares. Conceptually, an injunction against voting the shares therefore differs little from an injunction against future violations; sterilization merely forbids voting which, though legal in itself, is made possible by the illegal acquisition. In this respect sterilization resembles many remedies granted in other areas of administrative law.<sup>304</sup> It does not interfere with corporate governance in a way contrary to the intent of Congress.

Although a court should stay the SEC's suit for sterilization if a private suit for the same relief is pending and being competently pursued,<sup>305</sup> a court should be more reluctant to

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302. Where the SEC may pursue disgorgement, rescission, or restitution, it should also be able to obtain appointment of a trustee for the limited purpose of receiving funds from the defendants, evaluating claims by members of the injured class, and paying legitimate claims. This does seem to reduce the Commission to a collection agency. But if private actions are unavailable and the SEC obtains a monetary recovery from the defendant, it seems an insignificant extension of the Commission's powers and consistent with the purposes of the securities laws to arrange for the money recovered to be paid to the actual victims.

303. In 1975 Congress adopted section 21(g) of the Exchange Act, prohibiting the consolidation of SEC and private actions without the SEC's consent, because cases ordering such consolidation were deemed to have hindered SEC enforcement activities. Securities Acts Amendments of 1975, Pub. L. No. 94-29, § 17(3), 89 Stat. 155 (codified at 15 U.S.C. § 78u(g) (1976 & Supp. V 1981)). Neither the language nor the purpose of the amendment should bar a stay, however, if the reason for the stay is that effective relief may be procured in private suits. As to procedures in such cases, see *infra* note 305.

304. See *supra* notes 64-70 and accompanying text (discussing the remedies of divestiture after an illegal merger and of corrective advertising).

305. When a private suit is pending, the court may handle a suit by the SEC somewhat as it would treat a second shareholder's derivative suit, deciding whether to stay or dismiss the SEC's suit or to permit it to proceed. See W. CARY & M. EISENBERG, *supra* note 299, at 970-72. Of course, a court cannot order that the SEC's suit be consolidated with a private suit. Securities Exchange

await a private suit here than in a restitution case. Sterilization of voting rights may affect all shareholders and not just the private plaintiffs. As such, the need for SEC involvement may be greater.

## 2. *Relief Pendente Lite*

Equity has long approved remedies *pendente lite* to preserve the jurisdiction of a court by maintaining the status quo or preventing the removal or dissipation of assets.<sup>306</sup> These remedies generally promote the purposes of the securities laws and should be permitted. The only such remedy that is problematic is the appointment of a receiver, which is discussed below.<sup>307</sup>

## 3. *Remedies to Prevent Future Violations—Removal and Appointment of Directors, Appointment of Special Agents and Special Counsel, Etc.*

The history of equity contains very little precedent for the appointment or removal of directors. Although a few state courts have suggested in dictum that they can remove a director,<sup>308</sup> actual cases of removal are extremely rare.<sup>309</sup> Cases of

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Act of 1934, § 21(g), 15 U.S.C. § 78u(g) (1976 & Supp. V 1981). See *supra* note 303.

306. FED. R. CIV. P. 64 provides for provisional remedies "for the purpose of securing satisfaction of the judgment ultimately to be entered in the action . . . under the circumstances and in the manner provided by" state law. These remedies "include arrest, attachment, garnishment, replevin, sequestration, and other corresponding or equivalent remedies . . ." Rule 64 codified long-standing federal practice. 7 J. MOORE, *supra* note 59, ¶ 64.03. FED. R. CIV. P. 65 provides for injunctive relief, including the provisional remedies of preliminary injunctions and temporary restraining orders. FED. R. CIV. P. 66 provides for receiverships. Provisional remedies may be used to maintain the status quo, as is apparent from the nature of these remedies, although maintenance of the status quo is not their sole purpose. D. DOBBS, *supra* note 298, at 109-10. See *supra* note 20 (securities cases granting injunctions *pendente lite*).

307. See *infra* notes 343-65 and accompanying text.

308. See *Feldman v. Pennroad Corp.*, 60 F. Supp. 716, 719 (D. Del. 1945), *aff'd*, 155 F.2d 773 (3d Cir. 1946), *cert. denied*, 329 U.S. 808 (1947) (diversity case; no removal unless directors guilty of fraud); *Gettinger v. Heaney*, 220 Ala. 613, 617, 127 So. 195, 198 (1930) (no removal unless other remedies inadequate); *DeGarmo v. Goldman*, 19 Cal. 2d 755, 760-61, 123 P.2d 1, 4 (1942) (respondent seeking removal of directors must come to court of equity with clean hands); *Nahikian v. Mattingly*, 265 Mich. 128, 135, 251 N.W. 421, 424 (1933) (no removal unless directors guilty of fraud). See generally Brudney, *Fiduciary Ideology in Transactions Affecting Corporate Control*, 65 MICH. L. REV. 259, 281 (1966); Annot., 124 A.L.R. 364 (1940).

309. *Brown v. North Ventura Rd. Dev. Co.*, 216 Cal. App. 2d 227, 232, 30 Cal. Rptr. 568, 571 (1963), is the only case the author's research has disclosed. Even in that case not only did the court rely in part on a statute, but it also seemed

removal absent common law fraud and of judicial appointment of new directors are virtually nonexistent.<sup>310</sup> Many state courts have denied that equity empowers them to remove directors.<sup>311</sup> There is no precedent for such relief in other areas of administrative law, and no support for it in the legislative history of the securities laws.

Restructuring corporate boards also contravenes the intention of Congress in several important respects. First, such relief intrudes improperly into corporate governance. Although Congress intended the securities laws to affect corporate governance, it intended their influence to be indirect—a result of disclosure and shareholder suffrage rather than of direct Commission regulation.<sup>312</sup> Directors participate in all major corporate business decisions; securities compliance occupies little of their time. Restructuring corporate boards therefore necessarily involves both the SEC and the courts in the business policies of the affected corporation.

Second, restructuring corporate boards denies shareholder suffrage, which was a key principle of the Exchange Act.<sup>313</sup> Indeed, that is not only the effect of the Commission's activities but also its purpose. The Commission appoints its own candidates to the board without a shareholder election, and sometimes even prevents shareholders by court decree from removing or failing to reelect the SEC's board candidates for several years.<sup>314</sup> Moreover, the shareholders' franchise is usually eliminated without any meaningful representation of shareholders in the judicial proceeding. In theory, corporate management represents shareholder interests. In practice, the managers lose little by surrendering the shareholders' franchise, and in so doing they may placate the SEC and avoid

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that the plaintiff was enjoined from acting as a director because he had not been duly elected, rather than being removed from a directorship. *Id.* at 231-32, 30 Cal. Rptr. at 570. There have been a few cases (though even these are rare) removing a director pursuant to statute, but of course these cases provide no authority for a general equitable power to remove directors. *See, e.g.,* *People v. Lyon*, 119 A.D. 361, 362, 104 N.Y.S. 319, 320 (1907) (proceeding by attorney general pursuant to statute); *Markovitz v. Markovitz*, 336 Pa. 145, 148-49, 8 A.2d 46, 48 (1939) (director removed pursuant to statute; court stated that prior to statute it could not remove directors).

310. While the author's research has disclosed no such case, he is not prepared to state flatly that none exists.

311. *See, e.g.,* *Neall v. Hill*, 16 Cal. 146, 149 (1860); *In re Burkin*, 1 N.Y.2d 570, 573-74, 136 N.E.2d 862, 865, 154 N.Y.S.2d 898, 901-02 (1956).

312. *See supra* notes 173-81 and accompanying text.

313. *See supra* notes 175-77 and accompanying text; Comment, *Tailor the Director*, *supra* note 4, at 527-29.

314. *See supra* note 39, *infra* note 320 and accompanying text.

litigation that might do the managers greater personal harm.<sup>315</sup> In theory, the SEC also represents shareholder interests. Its approval of, and indeed its fond wish for, decrees eliminating shareholder rights belies the theory. Although many commentators concede that the ideal of shareholder democracy is unattainable,<sup>316</sup> the SEC cannot ignore shareholder suffrage to pursue its own theories of corporate governance. Congress established the principle of shareholder suffrage, and if that principle is to be abandoned, Congress must do so.

Finally, as a corollary to the first two points, restructuring corporate boards violates the intent of Congress that corporations, especially in their internal affairs, be governed by state law except where clearly preempted by the federal securities laws.<sup>317</sup> State corporation laws provide that a corporation shall be managed by a board of directors elected and subject to removal by the shareholders.<sup>318</sup> Directors owe shareholders fiduciary duties which may be enforced by shareholder derivative suits or class actions.<sup>319</sup> Selection and removal of directors by the SEC<sup>320</sup> thus violates the principle of state control as

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315. Farrand, *supra* note 4, at 1806 n.143, notes that the interests of the SEC enforcement staff and of corporate insiders may coincide in favor of ancillary relief, to the detriment of shareholders. The staff often prefers a quick consent decree to protracted litigation because it saves time and can be categorized as a victory. Corporate management may also prefer a quick settlement that minimizes adverse publicity and disruption and, more important, reduces or eliminates the danger that further investigation will result in a criminal indictment against insiders. "Moreover, depending on their stock holdings and other factors, such insiders may feel little hesitation in giving away shareholder powers and authorizing corporate expenditures of funds when negotiating with the SEC on possible ancillary remedies." *Id.*

316. See, e.g., Manning, *Thinking Straight About Corporate Law Reform*, 41 LAW & CONTEMP. PROBS. 3, 14 (Summer 1977) (shareholders are economically motivated and consequently are more likely to sell their shares if they become disenchanted, rather than vote them). Some find this not only inevitable but desirable. See Chayes, *The Modern Corporation and the Rule of Law*, in THE CORPORATION IN MODERN SOCIETY 41 (Mason ed. 1959) (shareholders "deserve the voiceless position in which the modern development left them").

317. See *supra* notes 188-91 and accompanying text. The Supreme Court has recognized this in *Santa Fe* and elsewhere. See *supra* notes 226-40 and accompanying text.

318. See W. CARY & M. EISENBERG, *supra* note 299, at 140; H. HENN, *HANDBOOK OF THE LAW OF CORPORATIONS* § 192, at 376 (2d ed. 1970).

319. H. HENN, *supra* note 318, §§ 231-42, at 450-83, §§ 358-76, at 749-94.

320. When directors are appointed by a court, shareholders lose their power to elect directors. See *supra* notes 29, 36. Decrees also bar the shareholders from removing court-appointed directors and, sometimes, from electing any additional directors. See Comment, *Equitable Remedies*, *supra* note 4, at 1205-06 (quoting final judgment in *SEC v. Vesco*, 72 Civ. 5001 (S.D.N.Y. Mar. 16, 1973); *supra* note 39. This disenfranchisement may last well beyond the usual one year term for elected directors. In *SEC v. Mattel, Inc.*, the court appointed directors for five years. See *supra* text accompanying note 36. To accomplish its



well as shareholder suffrage. Many decrees also violate the principle of board management<sup>321</sup> and immunize the court-appointed directors from certain liabilities to shareholders under state law.<sup>322</sup> In short, such relief violently displaces state law in an area where Congress intended state law to prevail.

To permit the SEC and the district courts to restructure corporate boards would set a precedent difficult to contain in other important areas. First, if the SEC can restructure corporate boards through ancillary relief, why could it not do the same by rule? The SEC has justified restructuring through ancillary relief by findings that such relief is necessary to ensure compliance with the securities laws by a corporation that has violated them. Suppose the SEC concluded that, in order to raise securities compliance to an acceptable level, it should by rule require that each public corporation have several overview committees composed solely of outside directors and a board with no insiders except the chief executive officer, who would not be the board chairman.<sup>323</sup> Given the great deference courts afford the factual underpinnings of agency rules,<sup>324</sup> such a rule could not be attacked for lacking factual support. The only other possible objections to such a rule would be that it intrudes improperly into corporate governance, denies shareholder suffrage, and interferes with state corporation laws—the

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objectives the Commission may also have a corporation's by-laws amended without the usual requisite vote of shareholders or directors. *See supra* note 32. This disenfranchisement could reduce the value of the corporation's shares. *See DeMott, Reweaving the Corporate Veil: Management Structure and the Control of Corporate Information*, 41 LAW & CONTEMP. PROBS. 182, 190 n.44 (Summer 1977).

321. Ancillary relief decrees often divest the board of certain managerial powers and vest those powers instead in a special counsel or special agent. *See supra* notes 27, 28, 36. Many decrees have also limited the board's managerial discretion by requiring the adoption of special procedures or forbidding the corporation to act in ways not otherwise illegal, such as forbidding it to enter new lines of business. *See supra* note 22.

322. *See* Final Judgment of Permanent Injunction and Appointment of Special Counsel and Directors ¶ 4(ii), SEC v. Vesco, 72 Civ. 5001 (S.D.N.Y. March 16, 1973) (providing that court-appointed directors not be liable for errors of judgment unless they were "grossly negligent").

323. Former SEC Chairman Harold Williams often advocated this board structure. *See* Williams, Corporate Accountability and Corporate Power (Oct. 24, 1979) (speech in the Fairness Lecture Series, Carnegie-Mellon University, Pittsburgh, Pa.).

324. Although a reviewing court may generally substitute its own judgment for that of an administrative agency as to questions of law, as to questions of fact a court may set aside agency action only if it is "arbitrary [or] capricious" or "unsupported by substantial evidence." Administrative Procedure Act § 10(e), 5 U.S.C. § 706(2) (1976); *Universal Camera Corp. v. NLRB*, 340 U.S. 474, 487-88 (1951); 4 K. DAVIS, ADMINISTRATIVE LAW TREATISE § 29.01, at 116-17 (1958).

same arguments made against restructuring corporate boards through ancillary relief. Indeed, the hypothetical rule is less objectionable than restructuring through ancillary relief because the latter, unlike the former, often involves the SEC in the actual selection of individual directors to the exclusion of the shareholders. It probably would be generally conceded that the SEC could not adopt such a rule. It follows that restructuring corporate boards through ancillary relief is also inappropriate.

Second, if the SEC can restructure corporate boards so as to obtain compliance with the securities laws, it is difficult to see why many other federal administrative agencies cannot obtain similar relief to ensure compliance with the statutes they oversee. Indeed, many have a stronger claim than the SEC that Congress did intend them to regulate the internal governance of regulated companies. Yet, to grant such relief regularly to other agencies would depart radically from tradition in administrative law.<sup>325</sup> Although this tradition might be ascribed to agency timidity, the more plausible explanation is that other agencies recognize that if Congress had intended them to have such power, it would have said so explicitly.

A final reason for rejecting the restructuring of corporate boards as ancillary relief is that other remedies can equally or more effectively ensure compliance with the securities laws. For purposes of deterring future violations, the impact of an injunction is substantial.<sup>326</sup> An injunction against a corporate defendant also binds its directors and officers.<sup>327</sup> If an injunction is not enough, the Commission may resort to its many other express remedies, such as suspending trading, suspending a 1934 Act registration statement, issuing public statements, or referring the case for criminal prosecution.<sup>328</sup> It is doubtful whether removing directors, appointing Commission-approved directors, requiring board majorities of outside directors, or imposing various overview committees dominated by outside directors no-

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325. See *supra* notes 59-77 and accompanying text.

326. See *supra* note 295 and accompanying text.

327. 10 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 4875, at 339 (rev. perm. ed. 1978). FED. R. CIV. P. 65(d) makes an injunction binding "upon the parties to the action, their officers, agents, servants, employees, and attorneys . . . ." See generally 7-2 J. MOORE, *supra* note 59, ¶ 65.13 (discussing persons bound by injunctions and restraining orders under rule 65(d)).

328. See *supra* notes 150, 156-60 and accompanying text. Against securities professionals the SEC has further remedies. See *supra* notes 161-64 and accompanying text.

ticeably will improve a corporation's compliance with the securities laws. There is little empirical evidence that outside directors or overview committees improve board performance generally, and no evidence that they improve compliance with securities laws.<sup>329</sup> Even theoretical discussions question whether these conditions can improve corporate governance.<sup>330</sup> Indeed, some believe that inside boards perform better than outside boards.<sup>331</sup> Corporate boards often lack effective control over corporate disclosure,<sup>332</sup> so it is questionable whether restructuring the board improves disclosure. In sum, the Commission has potent express remedies for compelling corporate securities compliance, and there is little inductive or empirical basis for believing that restructuring corporate boards improves compliance with securities laws or corporate governance generally.

If ancillary remedies are necessary to ensure future compliance, remedies short of restructuring the board may be appropriate. For example, in many cases the SEC has obtained the appointment of a corporate officer with special duties and powers relating to disclosure or the imposition of special procedures that, while not otherwise required by law, will help promote full disclosure.<sup>333</sup> Because the special agent or special

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329. See Brudney, *The Independent Director—Heavenly City or Potemkin Village?*, 95 HARV. L. REV. 597, 616-22 (there is little evidence that outside directors improve management integrity), 635 (there is little evidence that outside directors improve management efficiency) (1982); DeMott, *supra* note 320, at 220-21; Solomon, *Restructuring the Corporate Board of Directors: Fond Hope—Faint Promise?*, 76 MICH. L. REV. 581, 588-89, 610 (1978).

330. See Brudney, *supra* note 329, at 607-16, 632-34; Dent, *The Revolution in Corporate Governance, The Monitoring Board, and the Director's Duty of Care*, 61 B.U.L. REV. 623, 663-81 (1981). It has also been questioned whether directors appointed by the courts and the SEC will have the necessary profit motive. See Wolfson, *Needed: Statutory Reform to Improve Consent Decree Process*, 57 HARV. BUS. REV. (Mar.-Apr. 1979).

331. See S. VANCE, *THE CORPORATE DIRECTOR* 5 (1968); S. VANCE, *BOARDS OF DIRECTORS: STRUCTURE AND PERFORMANCE* 5 (1964); Schmidt, *Does Board Composition Really Make a Difference?*, 12 CONF. BD. REC. 38 (Oct. 1975). But see H. KOONTZ, *THE BOARD OF DIRECTORS AND EFFECTIVE MANAGEMENT* 129-32 (1967) (identifying advantages of outside directors).

332. Since outside directors do not conduct corporate operations and lack the staff to monitor operations, they have only the information management gives them. The outsiders cannot disclose what they do not know, and the recent series of improper payments scandals demonstrated that often outsiders were kept ignorant of the payments. See Coffee, *supra* note 242, at 1127-29, 1264-65. Moreover, even where the board does have information, disclosure documents are drafted under the direction of management, and the outside directors usually see the documents only after they have been released. Thus, management controls not only the substance but also the form of disclosure.

333. See cases cited *supra* note 28.

procedure deals specifically with disclosure, it can be more effective than placing SEC nominees or other outside directors on the board.<sup>334</sup> Often, disclosure violations cannot be traced to specific corporate officers, so that only the corporation itself can be punished. This remains true even if the corporation is subject to an injunction or has a board restructured through ancillary relief. But a court may reasonably refuse to impose on a corporation a heavy fine that will ultimately injure the shareholders—the very persons the securities laws were intended to protect. By focusing the obligation of disclosure on certain persons, special agents or procedures can make an injunction more effective.

Is the imposition of special agents and procedures an appropriate remedy under the federal securities laws? There is very little precedent for such remedies in the history of equity or in other areas of administrative law<sup>335</sup> and no direct support for them in the legislative history. As just noted, however, they do promote the purposes of the federal securities laws. Moreover, they do not interfere with corporate governance, with shareholder suffrage, or with state law to the same extent as the restructuring of corporate boards. Although imposition of special agents or procedures does usurp the board's managerial prerogatives, the usurpation is slight and is limited to the legitimate scope of the securities laws. Moreover, it does not violate shareholder suffrage and the fiduciary duties and liabilities of directors to shareholders. Accordingly, these ancillary remedies should be permitted. Nevertheless, because they do intrude somewhat into corporate governance, impose on the corporation burdens heavier than the law otherwise demands, and have not traditionally been granted, a court should award these remedies only in unusual cases where it is persuaded that an injunction alone will not assure compliance. If additional disclosure burdens are to be imposed routinely on issuers, they should be imposed by statute or by SEC rules promulgated pursuant to statutory authority.

A last ancillary remedy affecting future corporate behavior is the appointment of special counsel to investigate past securities law offenses and to sue thereon on behalf of the corporation. Arguably, this practice is necessary to effective

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334. The latter approach is unlikely to be effective because directors, especially outside directors, usually do not control corporate disclosure. *See supra* note 332.

335. *See supra* notes 59-77 and accompanying text.

enforcement of the securities laws because the Commission is understaffed.<sup>336</sup> Although there is almost no precedent for such relief in equity or other areas of administrative law<sup>337</sup> and no support for it in the legislative history, it does promote enforcement of the securities laws.<sup>338</sup> One might argue either that in setting the Commission's budget Congress has deliberately limited its enforcement activities or that the SEC has not efficiently deployed its enforcement resources.<sup>339</sup> There are many reasons for limiting an agency's budget, however, and it seems unlikely that Congress intends by its budgets to permit many securities law violations to go unpunished. Further, the Commission's resources, even if more efficiently utilized, would not suffice to pursue all serious securities law violations.

Appointment of special counsel raises two problems, however. First, a corporate decision whether to sue involves the exercise of business judgment not only as to the prospects of success but also as to the impact of the suit on the corporation. Often a corporation reasonably decides that it does not serve its interests to press a claim that is probably meritorious.<sup>340</sup> When a court appoints a special counsel, usually with instructions not to abandon or to compromise any claim without the SEC's consent, the board loses its power under state law to decide whether to sue.

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336. The SEC often complains that it is understaffed. See *S.E.C. Warns on Budget Cut*, N.Y. Times, Oct. 16, 1981, at D1, col. 6 (in response to proposed budget cuts, Chairman Shad "complained that the agency was already 'thinly staffed' . . ."). Commentators have often cited staff limitations as a reason the Commission settles so many cases. See Mathews, *SEC Civil Injunctive Actions—II*, 5 REV. SEC. REG. 949, 955 (1972); Wolfson, *supra* note 330, at 19; Comment, *Equitable Remedies*, *supra* note 4, at 1192. Appointment of special counsel is especially attractive to the SEC in this regard because it permits investigation and perhaps litigation to continue without using staff resources. Note, however, that the Commission's staff shortage is not reason enough to justify an implied remedy. *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1, 41 (1977).

337. See *supra* notes 59-77 and accompanying text.

338. A priori, any additional amount of enforcement should help deter future violations. Given that the SEC staff is fully occupied, private suits provide additional enforcement. Given the general behavior of insiders when fellow insiders are accused of wrongdoing, see Brudney, *supra* note 329, at 611-13, 616-22, private suits prosecuted by disinterested outside counsel approved by the SEC are probably more effective than suits brought by regular corporate counsel controlled by the board and management. See Coffee, *supra* note 77, at 455.

339. It has been suggested that the SEC makes poor use of its resources. See H. KRIPKE, *supra* note 140, at 51.

340. Courts have upheld the refusal of corporate boards to sue and their decision to oppose derivative suits on the corporation's behalf for reasons other than the merits. See *Maldonado v. Flynn*, 485 F. Supp. 274, 285 (S.D.N.Y. 1980); *Gall v. Exxon Corp.*, 418 F. Supp. 508, 514 n.13 (S.D.N.Y. 1976); *Falkenberg v. Baldwin*, N.Y.L.J., Mar. 3, 1980, at 12, col. 6 (Sup. Ct. 1980).

Second, court appointment of special counsel to pursue securities law violations involves a questionable delegation or, as Professor Kripke has phrased it, "franchising"<sup>341</sup> of the Commission's enforcement powers. That no other federal agency or department engages in this practice in itself counsels caution. More fundamentally, powers conferred by Congress on a government agency are subject to democratic control, including presidential veto and the congressional budgetary process. Appointment of special counsel to be paid by a corporation evades these controls. Not only does the SEC delegate its own authority but the judiciary arrogates legislative prerogatives by cooperating in this delegation.<sup>342</sup> Even if the constitutional principle of the separation of powers does not absolutely forbid such appointments, certainly courts should not impose such appointments on an unwilling corporation absent clear congressional authorization.<sup>343</sup>

#### 4. Receiverships

The Commission has argued that, because it can obtain a receiver, a fortiori it can obtain the less drastic remedy of the removal or appointment of directors.<sup>344</sup> Although this Article has rejected the court-imposed restructuring of corporate boards, it does not necessarily follow that a court may not appoint receivers. A receivership is traditionally granted only in extreme circumstances and is not a more drastic remedy than the restructuring of a corporate board because of the limited functions of a receiver.

Although the receivership is a traditional equitable remedy, equity has strictly limited the conditions in which a receiver would be appointed. First, the plaintiff must show

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341. This term has been used by Professor Kripke in his seminar on securities law at New York University School of Law. Such delegation is probably not unconstitutional, but it does run counter to the spirit of the constitutional doctrine of the separation of powers. See *infra* notes 400-01.

342. Court approval is crucial. Without it the SEC would have only an agreement of the corporation. The SEC's only remedy for breach of this agreement might be reinstitution of the original suit, which may already have grown stale.

343. The corporation's consent may necessitate different conclusions. See *infra* note 379 and accompanying text.

344. See Sporkin, *supra* note 4, at 123; Comment, *Court Appointed Directors*, *supra* note 4, at 741. Cf. Brief for the Appellee at 23, SEC v. Beisinger Indus. Corp., 552 F.2d 15 (1st Cir. 1977) ("the circumstances warranting the appointment of [a special] agent need not be as serious as might be required for the appointment of a receiver"). But see Comment, *Equitable Remedies*, *supra* note 4, at 1210-12. For securities cases granting receivers, see *supra* note 21.

preliminarily some existing legal right "amounting to more than a mere claim" to assets held by the defendant.<sup>345</sup> Second, there must be serious danger of waste or dissipation of these assets before final disposition of the case.<sup>346</sup> Third, there must be no lesser remedy adequate to protect the plaintiff's claim.<sup>347</sup> In general, a receivership is to be granted only in extreme circumstances because a receivership deprives the defendant of property before a final judgment.<sup>348</sup>

Even more important than the conditions to the appointment of a receiver are the traditional limitations on the functions of a receiver that flow from two principles. First, receivership is only a provisional, subsidiary remedy to prevent the dissipation of assets before a final judgment can be entered, a final remedy granted, and assets distributed accordingly.<sup>349</sup> Second, a receiver is an officer of the court.<sup>350</sup> The court in ef-

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345. *Mintzer v. Arthur L. Wright Co.*, 263 F.2d 823, 825 (3d Cir. 1959). See *Kelleam v. Maryland Cas. Co.*, 312 U.S. 377, 380-82 (1941); 1 R. CLARK, *THE LAW OF RECEIVERS* §§ 49, 190 (3d ed. 1959); 3 *id.*, §§ 732.2, 732.3; 16 W. FLETCHER, *CYCLOPEDIA OF THE LAW OF CORPORATIONS* § 7687, at 78 (rev. perm. ed. 1979); 7-2 J. MOORE, *supra* note 59, ¶ 66.05[1], at 1920.1. Indeed, some older cases suggest that those claiming property as creditors must first show that they have no adequate remedy at law by obtaining a judgment, securing a writ of execution, and perhaps even having the writ returned unsatisfied. *Id.* at 1920.4-26. The existence of fraud is not by itself sufficient. 1 R. CLARK, *supra*, § 181.

346. See 3 R. CLARK, *supra* note 345, §§ 732.2, 732.3; 7-2 J. MOORE, *supra* note 59, ¶ 66.05[1], at 1920.1. Although the older cases often insisted on the defendant's insolvency as a condition to a receivership, most securities cases have dropped this requirement. See *SEC v. Bowler*, 427 F.2d 190, 198 (4th Cir. 1970); *SEC v. Keller Corp.*, 323 F.2d 397, 403 (7th Cir. 1963); *SEC v. Heritage Trust Co.*, 402 F. Supp. 744, 753 (D. Ariz. 1975). But see *Los Angeles Trust Deed & Mortgage Exch. v. SEC*, 264 F.2d 199, 206-07 (9th Cir. 1959) (appointment of receiver reversed in part for want of proof of insolvency). Insolvency may be relevant to whether a receiver is needed. 1 R. CLARK, *supra* note 345, § 182, at 265.

347. See 1 R. CLARK, *supra* note 345, § 59; 3 *id.*, §§ 744, 784; 16 W. FLETCHER, *supra* note 345, §§ 7708, 7727, 7729.

348. See *SEC v. Bartlett*, 422 F.2d 475, 478 (8th Cir. 1970); 1 R. CLARK, *supra* note 345, §§ 49, 54; 16 W. FLETCHER, *supra* note 345, § 7697; 7-2 J. MOORE, *supra* note 59, ¶ 66.05[1] at 1920.2; 12 C. WRIGHT & J. MILLER, *FEDERAL PRACTICE AND PROCEDURE* § 2983 (1973). In several reported securities cases courts have denied requests for a receiver. See *SEC v. Brigadoon Scotch Distrib., Ltd.*, 388 F. Supp. 1288, 1293 (S.D.N.Y. 1975); *SEC v. Republic Nat'l Life Ins. Co.*, 378 F. Supp. 430, 437-38 (S.D.N.Y. 1974). In general, corporate mismanagement is not a ground for appointment of a receiver. 16 W. FLETCHER, *supra* note 345, § 7714, at 161.

349. See *Gordon v. Washington*, 295 U.S. 30, 37 (1935); 1 R. CLARK, *supra* note 345, §§ 12-14, 17, 46, 51; 16 W. FLETCHER, *supra* note 345, § 7683; 7-2 J. MOORE, *supra* note 59, ¶ 66.03, at 1907-08. Similarly, a receivership is never an end in itself, but only a means to reach some legitimate end of equity: "a federal court of equity should not appoint a receiver where the appointment is not a remedy auxiliary to some primary relief which is sought and which equity may appropriately grant." *Kelleam v. Maryland Cas. Co.*, 312 U.S. 377, 381 (1941).

350. See *SEC v. Lincoln Thrift Ass'n*, 557 F.2d 1274 (9th Cir. 1977); 4 J. POME-

fect impounds assets subjected to a receivership, and since the judge (or chancellor) cannot personally manage these assets the court appoints someone—the receiver—to do so. Accordingly, the receiver is customarily limited to preserving the status quo pendente lite,<sup>351</sup> preventing the dissipation of assets,<sup>352</sup> conducting investigations,<sup>353</sup> collecting assets and paying claims,<sup>354</sup> and winding up the business.<sup>355</sup> To preserve the defendant's property, the receiver may be required to continue the defendant's business temporarily,<sup>356</sup> but a receivership is never a final remedy and should not continue longer than necessary to decide the case and distribute the defendant's property as ordered by the court.<sup>357</sup>

The SEC never satisfies the traditional conditions for a receivership because it never has an interest in or even a claim to property of a defendant. Even if the Commission can be viewed as standing in the shoes of investors, rarely would it be

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ROY, *supra* note 5, § 1330, at 923 (a receiver is "a quasi officer or representative of the court").

351. See *Los Angeles Trust Deed & Mortgage Exch. v. SEC*, 285 F.2d 162, 181 (9th Cir. 1960), *cert. denied*, 366 U.S. 919 (1961); 1 R. CLARK, *supra* note 345, §§ 12-14; 7-2 J. MOORE, *supra* note 59, ¶ 66.03, at 1907.

352. See *SEC v. Charles Plohn & Co.*, 433 F.2d 376, 379 (2d Cir. 1970); *SEC v. Bartlett*, 422 F.2d 475, 477-78 (8th Cir. 1970); *SEC v. H.S. Simmons & Co.*, 190 F. Supp. 432, 433 (S.D.N.Y. 1961); 1 R. CLARK, *supra* note 345, § 48; 16 W. FLETCHER, *supra* note 345, §§ 7665, 7725, 7813. The purpose of preserving assets is to prevent the defeating of the jurisdiction of the court. 1 R. CLARK, *supra* note 345, § 51.

353. See *SEC v. Koenig*, 469 F.2d 198 (2d Cir. 1972).

354. *SEC v. Western Pacific Gold & Silver Exch. Corp.*, [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,064, at 97,734-36 (D. Nev. 1975). See *Decker v. Independence Shares Corp.*, 311 U.S. 282, 285, 287-88 (1940); 1 R. CLARK, *supra* note 345, § 27.

355. See *Esbitt v. Dutch-American Merc. Corp.*, 335 F.2d 141, 143 (2d Cir. 1964) (receivership should not continue longer than necessary to get estate into bankruptcy); 2 R. CLARK, *supra* note 345, § 396 (receivership should not continue longer than necessary to wind up business or return it to original owner).

356. See, e.g., *SEC v. R.J. Allen & Assocs., Inc.*, 386 F. Supp. 866, 878-79 (S.D. Fla. 1974) (setting forth duties of receiver). See 7-2 J. MOORE, *supra* note 59, ¶ 66.03, at 1908; 2 R. CLARK, *supra* note 345, § 396, at 672 ("the only justification for a court making an order to a receiver to continue the business of a private corporation is to preserve . . . money, funds or property by so doing").

357. "The court should not use a receivership to continue indefinitely an enterprise that does not show evident signs of working out for the benefit of creditors." 7-2 J. MOORE, *supra* note 59, 66.04[7] (citing *Jones v. Village of Proctorville*, 332 F.2d 419 (6th Cir. 1964)). See 1 R. CLARK, *supra* note 345, §§ 26, 54, 166; *id.*, § 51, at 55 ("The purpose of the appointment of a receiver after judgment is to satisfy the judgment in one way or another."); 2 *id.*, § 396, at 673 ("Ordinarily a business should not be continued any longer than is necessary to properly advertise and dispose of it as a going concern, or restore it to the original owner."); 16 W. FLETCHER, *supra* note 345, § 7705.



entitled to a receiver.<sup>358</sup> Nonetheless, courts have occasionally granted the SEC a receiver without discussing whether the traditional conditions have been met,<sup>359</sup> and it is not always clear that they have restricted receivers to their traditional functions.<sup>360</sup>

Should the courts ever appoint a receiver in a federal securities case? Although a receiver, by taking complete control of a corporation, necessarily supplants corporate management and eliminates shareholder suffrage, the remedy is justified when the traditions of equity are observed. Since the receivership is only temporary, the interference with corporate governance and shareholder suffrage is limited. Because the traditions of equity are generally consistent with state law, appointment of a receiver should not interfere unduly with state law. Since the receivership is a traditional equitable remedy, Congress may have contemplated that it would be used in securities law. Most important, the receivership, if granted only in compelling circumstances, promotes the purposes of the securities laws. Those statutes were enacted to protect investors, and a receivership protects investors when there is danger of dissipation of assets to which they have a right and no lesser remedy will suffice.

Should a court ever appoint a receiver where the customary conditions are not met? If a receiver is unnecessary to prevent dissipation of assets to which investors have a right or if a lesser remedy will suffice, then the remedy should be unnecessary to promote the purposes of the securities laws. It is diffi-

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358. For example, rarely would an investor have an existing right "amounting to more than a mere claim" in assets held by the defendant. *See supra* note 345 and accompanying text. *See also* Farrand, *supra* note 4, at 1788 (SEC often fails to meet traditional criteria for receivership).

359. In *SEC v. Heritage Trust Co.*, 402 F. Supp. 744 (D. Ariz. 1975), the court granted an injunction but denied a receiver, in part because the corporation was solvent and meeting its obligations. *Id.* at 751. On the SEC's motion for clarification, a receiver was appointed. *Id.* at 752-54. The SEC showed further false and misleading statements, but the court made no findings as to, and did not even refer to, any new evidence of waste or dissipation of assets.

360. *See International Controls Corp. v. Vesco*, 490 F.2d 1334, 1340 (2d Cir.), *cert. denied*, 417 U.S. 932 (1974) (interim board appointed in lieu of receiver given full power to conduct corporate business). In *SEC v. Heritage Trust Co.*, 402 F. Supp. 744, 754 (D. Ariz. 1975), the court ordered the SEC to "submit . . . a proposed form of order for appointment of a receiver." This seems a bit strange because a receivership is only ancillary to some other primary remedy, *see supra* text accompanying note 349. That the court asked the plaintiff to propose a "form of order for appointment of a receiver" suggests that it may not have understood the purpose for and nature of the receivership. *See* Farrand, *supra* note 4, at 1787 & n. 53.

cult to imagine a threat short of dissipation of assets claimed by investors for which a receiver would be necessary. Congress cannot have contemplated such use of the receivership. Absent the customary conditions to and limitations on a receivership, all the objections to the restructuring of corporate boards would apply even more strongly to the receivership. Since restructuring is inappropriate, it follows a fortiori that, absent the customary conditions and limitations, a receivership would be inappropriate as well.

On occasion the receivership has been used to bring a corporation into compliance with the law.<sup>361</sup> This practice could invite abuse not only by enabling a court to displace corporate management with a receiver but also by providing the court a lever with which to extract corporate governance changes. For example, a court might be tempted to appoint (or to threaten to appoint) a receiver unless or until the corporation could show it would obey the securities laws. If the corporation knew or assumed that restructuring the corporate board was a condition to such a showing, the net result would be a restructuring of the board which the court could not order directly. Even assuming equity permits using a receivership to induce compliance, other less intrusive remedies should almost invariably suffice. Thus, if a corporation has failed to file certain financial reports properly, a special officer could be appointed with powers to compile and to file the reports without the managerial displacement that a receivership entails. This also comports with equity's command that a receiver not be appointed if a lesser remedy will suffice.

Can the restructuring of a corporate board also be such a lesser remedy? Since a receivership is a provisional remedy, any change would have to be temporary. Officers or directors appointed would be officers of the court who would need periodic court approval of past and future actions. Although they might continue the business, they could not, as court officers, substantially revise the business or undertake new ventures. Nonetheless, the drawbacks of a receivership to the sharehold-

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361. See *SEC v. S & P Nat'l Corp.*, 360 F.2d 741, 750-51 (2d Cir. 1966) (Investment Company Act case; one purpose of receiver was to bring defendant into compliance with the law). See also *SEC v. Koenig*, 469 F.2d 198 (2d Cir. 1972) (limited receiver appointed to take certain actions necessary under the securities laws); *Los Angeles Trust Deed & Mortgage Exch. v. SEC*, 285 F.2d 162, 181 (9th Cir. 1960), *cert. denied*, 366 U.S. 919 (1961) (receiver appointed "until such time as the appellants can comply with the law").

ers,<sup>362</sup> the intended benefactors, spur the search for alternatives when the incumbent board threatens to injure investors and appointment of a special disclosure officer or the like will not avert the danger. To tolerate board restructuring in such cases might create a loophole that could be abused if courts did not adhere carefully to the conditions and limitations of the receivership. If the court observes these conditions and limitations, however, and makes the findings necessary for the appointment of a receiver and clearly states that restructuring is being ordered as a more palatable substitute for a receivership, restructuring should be permitted, at least until experience shows that this option is being abused. The law does not bar the SEC or the courts from calling a receiver by another name so long as they do not violate the conditions and limitations of the receivership.<sup>363</sup>

Another issue is whether a court should vest a receiver with functions broader than those customary in equity. The traditional role of the receiver was tailored to the purpose of the receivership—to preserve assets pending litigation. To expand this role would require some new justification sufficiently compelling to overcome both the history of equity and congressional opposition to SEC interference with corporate governance and state corporation laws<sup>364</sup> and to denial of shareholder suffrage. No such justification exists, however.

In sum, when the SEC satisfies the customary requirements,<sup>365</sup> it should be able to obtain a receiver (however named) with the customary limited functions, and not otherwise.

### C. THE SIGNIFICANCE OF THE DEFENDANT'S CONSENT

The vast majority of court orders granting ancillary relief in securities law, especially those affecting internal corporate af-

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362. Appointment of a receiver may trigger the acceleration of the obligation to pay corporate debt, thereby precipitating a financial crisis, possibly insolvency, for the corporation. See Sporkin, *supra* note 4, at 123.

363. See *Braasch v. Muscat*, [1967-69 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 92,148, at 96,677 (S.D.N.Y.), *remanded*, 398 F.2d 1022 (2d Cir. 1968) (court appointed "special fiscal agent" to preserve assets).

364. So long as federal courts observe the traditional limitations of receivers, they are not unduly interfering with state law, which also generally observes these limitations. To expand these functions, however, involves supplanting a management selected under state law in a way inconsistent with state law.

365. Of course, investors rather than the SEC itself would have to have a claim to the defendant's assets. See *supra* text accompanying notes 345, 358.

fairs, have resulted not from contested proceedings but from consent decrees.<sup>366</sup> Even if the preceding analysis is correct in concluding that the securities laws do not authorize certain ancillary remedies, especially those intruding on corporate governance, one might argue that the defendant's consent constitutes a knowing waiver that cures the defect. A few cases have adopted this rationale when the defendant or a third party has attacked a consent decree.<sup>367</sup>

A consent decree is not merely a settlement between the defendant and the plaintiff; rather it is a court order with all the ramifications of an order issued after a contested proceeding.<sup>368</sup> Accordingly, before entering a consent decree, a court should exercise no less care than in a contested proceeding to ensure that the decree precisely fits the needs of the specific case.<sup>369</sup> A court is ill-equipped, though, to scrutinize a proposed consent

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366. Although the portion of ancillary relief cases that are settled has not been calculated, there is no reason to think that it is any less than the portion of all SEC cases that are settled. The latter has been estimated at about 90%. Interview with SEC Commissioner Irving Pollack, 484 SEC. REG. & L. REP. (BNA) AA-1, AA-4 (Jan. 3, 1979). See also 41 S.E.C. ANN. REP. 95, 98 (1975) (settlement as disposition of a case). No court has restructured a corporate board in a contested case. See *supra* note 29.

367. See *Handler v. SEC*, 610 F.2d 656, 659 (9th Cir. 1979); *International Controls Corp. v. Vesco*, 490 F.2d 1334, 1351-52 (2d Cir.), *cert. denied*, 417 U.S. 932 (1974). Outside the securities field, too, third-party attacks on consent decrees have been unsuccessful. See *McAleer v. American Tel. & Tel. Co.*, 416 F. Supp. 435, 438 (D.D.C. 1976); *Construction Indus. Combined Comm. v. International Union of Operat. Eng'rs*, 67 F.R.D. 664, 665 (E.D. Mo. 1975).

368. See *SEC v. Thermodynamics, Inc.*, 319 F. Supp. 1380, 1382 (D. Colo. 1970), *aff'd*, 464 F.2d 457 (10th Cir. 1972), *cert. denied*, 410 U.S. 927 (1973). Granting a consent decree is a judicial function. *SEC v. Dennett*, 429 F.2d 1303, 1304 (10th Cir. 1970); *United States v. Carter Prods., Inc.*, 211 F. Supp. 144, 147 (S.D.N.Y. 1962).

369. In considering a proposed consent decree the court should not be a "rubber stamp," *United States v. CIBA Corp.*, 50 F.R.D. 507, 514 (S.D.N.Y. 1970), but must determine whether the proposed decree is consistent with law and equity, *United States v. International Tel. & Tel. Corp.*, 349 F. Supp. 22, 25 n.2 (D. Conn. 1972), *aff'd sub nom. Nader v. United States*, 410 U.S. 919 (1973); *Boyd v. United States* 345 F. Supp. 790, 793 (E.D.N.Y. 1972); *United States v. Automobile Mfrs. Ass'n*, 307 F. Supp. 617, 620-21 (C.D. Cal. 1969); *United States v. Carter Prods., Inc.*, 211 F. Supp. 144, 147 (S.D.N.Y. 1962), and consistent with the public interest and the interests of third parties, *United States v. Carrols Dev. Corp.*, 454 F. Supp. 1215, 1222 (N.D.N.Y. 1978); *Boyd v. United States*, 345 F. Supp. at 792-93; *United States v. Automobile Mfrs. Ass'n*, 307 F. Supp. at 621, *United States v. Carter Prods., Inc.*, 211 F. Supp. at 147-48. Indeed, in some cases courts have refused to enter consent decrees without first modifying them. *Orth v. Transit Inv. Corp.*, 132 F.2d 938, 945 (3d Cir. 1942) (court refused to appoint receiver provided in consent decree); *United States v. American Tel. & Tel. Corp.*, 552 F. Supp. 131 (D.D.C. 1982) (court substantially revised terms of consent decree in antitrust case); *United States v. Ling-Temco-Vought, Inc.*, 315 F. Supp. 1301, 1308-10 (W.D. Pa. 1970) (consent decree adopted on condition of undertaking by parties to protect employee benefit and pension funds).

decree and to discover and weigh objections to the relief it provides.<sup>370</sup> Once the parties have closed ranks, the judge in an adversarial system cannot independently investigate the facts and probe any weaknesses in the parties' arguments.

The judge's difficulty in regulating consent decrees prior to entry magnifies the importance of determining when a consent decree can later be modified or terminated. The defendant or a third party may attack a consent decree because the decree either was improper when issued or has become improper through changed circumstances. Most courts balk at modifying or terminating consent decrees, especially for claims of initial impropriety. To obtain relief in the latter case one must show that the original decree was procured by fraud or without actual consent, or that the court lacked subject matter jurisdiction.<sup>371</sup>

There are good reasons to reconsider this position, at least as to consent decrees granting ancillary relief in securities cases. First, not too much should be made of the defendant's consent. Although wealthy defendants may even enjoy an advantage over the SEC's understaffed and sometimes inexperienced enforcement division, the SEC usually possesses

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370. See *United States v. CIBA Corp.*, 50 F.R.D. 507, 514 (S.D.N.Y. 1970) (recognizing that "the court's time, talents and resources for intensive scrutiny are severely limited"). A similar situation is presented in the settlement of shareholder's derivative suits, which must be approved by the court under the Federal Rules and the rules of most states. See W. CARY & M. EISENBERG, *supra* note 299, at 975. The problems were noted in *Alleghany Corp. v. Kirby*, 333 F.2d 327, 347 (2d Cir. 1964) (Friendly, J., dissenting) ("Once a settlement is agreed, the attorneys for the plaintiff stockholders link arms with their former adversaries to defend the joint handiwork . . . . The stockholders' true representative was the court, which was allowed to proceed in ignorance of vital information."), *aff'd en banc by an equally divided court*, 340 F.2d 311 (2d Cir.), *cert. granted*, 381 U.S. 933 (1965), *dismissed*, 384 U.S. 28 (1966).

371. See *Swift & Co. v. United States*, 276 U.S. 311, 325-32 (1928) (lack of factual support and errors of law held not grounds for overturning consent decree, but "want of power to decide" and perhaps vagueness would be); *V.T.A., Inc. v. Airco, Inc.*, 597 F.2d 220, 226 (10th Cir. 1979) (private proceeding); *Walling v. Miller*, 138 F.2d 629, 632-33 (8th Cir. 1943), *cert. denied*, 321 U.S. 784 (1944) (district court's lack of power to grant restitution in suit by federal agency (as opposed to suit by employees) did not support collateral attack on consent decree). *Cf. NLRB v. Ochoa Fertilizer Corp.*, 368 U.S. 318, 323 (1961) (court could not modify decree as consented to when statute expressly prohibited such modification).

Under FED. R. Crv. P. 60(b) a court may modify or vacate a final judgment on several grounds, including when "the judgment is void;" "it is no longer equitable that the judgment should have prospective application;" or "any other reason justifying relief from the operation of the judgment." As suggested by the cases cited above, provision for relief that could not be awarded in a contested proceeding is not generally considered an adequate ground for relief under rule 60(b).

substantial leverage—some have said “overwhelming leverage”<sup>372</sup>—because of the great time, cost, and effort required of defendants to contest such proceedings, the damage from publicity over lengthy enforcement proceedings,<sup>373</sup> the possible collateral estoppel effect of an adverse contested judgment,<sup>374</sup> and fear that the Commission will argue that failure to consent signifies incorrigibility.<sup>375</sup> Defendants may accede to a quick consent decree, often filed with the SEC’s complaint, even though they genuinely believe either that they have not violated the law or that the SEC is not entitled to the relief to which they have consented. Some believe that the Commission pressures attorneys to persuade their clients to consent.<sup>376</sup>

Second, and more important, SEC enforcement proceedings, like the entire operation of the federal securities laws, affect the public interest. A consent decree may affect many persons other than the parties, especially corporate shareholders, whom the securities laws were intended to protect.<sup>377</sup> In negotiating a consent decree with the SEC, corporate management, which may have caused the securities law violation, may willingly sacrifice the corporation’s and the shareholders’ interests to the SEC’s desires to regulate corporate governance so as to avoid more serious personal liability.<sup>378</sup> Thus the courts must protect others against inappropriate relief, perhaps assisted occasionally by a disgruntled shareholder. In most cases, however, the court will be on its own, and in light of the difficulties of judicial scrutiny of consent decrees, courts should rely on rather broad, bright-line rules in choosing ancillary remedies. Accordingly, courts simply should not grant relief they could not grant in a contested case, despite the defend-

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372. Coffee, *supra* note 242, at 1252; Kripke, *supra* note 158, at 194.

373. Freedman & Sporkin, *supra* note 277, at 784-85 (comments of Professor Freedman). See also Kripke, *supra* note 158, at 189-90, 194-98, and authorities cited at 194 n.95.

374. See *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 332-33 (1979) (defendant in a civil damage action is collaterally estopped to relitigate issues of fact previously decided adversely to it in an SEC injunctive action).

375. The Commission often argues that by denying wrongdoing a defendant demonstrates a likelihood of future violations. See H. KRIPKE, *supra* note 140, at 50.

376. See *id.* at 22-23.

377. Corporate shareholders are most obviously affected by the removal and appointment of directors or the appointment of a receiver without their consent, but they are also affected, as owners of the corporation, by remedies that affect the corporation only financially, such as rescission, disgorgement, and restitution. As to the purpose of the securities laws to protect investors, see *supra* notes 173, 181 and accompanying text.

378. See *supra* note 315.

ant's consent. For the same reasons, a court should be willing to rescind a prior consent decree containing relief that the SEC was not entitled to obtain.

The reluctance to grant relief based on the defendant's consent should not apply equally to the appointment of special counsel to investigate and to sue on behalf of the corporation for violations of the securities laws.<sup>379</sup> The objections to granting this relief in contested cases differ from the objections to other remedies. Most objections to the special counsel remedy do not apply when the defendant consents to it. The decision to consent to the appointment of the special counsel is itself a business judgment. Corporations are generally free to litigate wrongs committed against them, and when a corporation agrees to do so in a consent decree there is no substantial usurpation of congressional authority to confer enforcement powers on governmental agencies.

## VI. THE ALI FEDERAL SECURITIES CODE AND A PROPOSED LEGISLATIVE APPROACH

Both because of the confusion that currently surrounds the issue of the propriety of ancillary relief in federal securities law and because Congress may soon reexamine the federal securities laws in connection with the American Law Institute's Federal Securities Code, it is appropriate to examine the Code's treatment of ancillary relief.

Section 1819(l) of the proposed Code provides:

ANCILLARY RELIEF—In a civil action created by or based on a violation of this Code, whether or not brought by the Commission, the court has the authority of a court of equity to grant appropriate ancillary or other relief, including an injunction, an accounting, a receivership of the defendant or the defendant's assets, disgorgement of profits, and restitution.<sup>380</sup>

Comment (1) to this section states that "[e]xcept for . . . the extension of the ancillary relief concept to actions traditionally at law, this codifies the case law."<sup>381</sup>

The drafters of the Code, particularly its reporter, Professor Louis Loss, deserve praise for addressing ancillary relief directly in the statute rather than leaving the courts to handle the issue on the basis of a mass of complex and often conflicting considerations. The Code leaves open many questions,

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379. See *supra* notes 336-43 and accompanying text.

380. 2 ALI FED. SECS. CODE 929 (1980).

381. *Id.*

however, primarily because of ambiguities in section 1819(l) and its comments.

A principal question is whether the Code approves such ancillary remedies as the removal or appointment of directors and the appointment of special counsel. These remedies are not specifically listed in section 1819(l). Comment (1) states that this section "codifies the case law," but as this Article has pointed out the case law is now unclear on many remedies, especially in contested cases. The provision confers on federal courts "the authority of a court of equity" to grant ancillary relief. This might be deemed to reject remedies not traditionally granted by equity, such as the restructuring of a corporate board. Section 1819(l) authorizes "appropriate ancillary or other relief," however, without excluding remedies that affect corporate governance. Comment (2) states not only that the "enumerated types of relief are not exclusive" but also that there is precedent for, *inter alia*, appointing a special counsel.<sup>382</sup> Moreover, prior commentators have usually concluded that courts may grant such relief. Accordingly, this section could also be deemed to authorize such remedies if the court believes them "appropriate" in a given case.

Section 1819(l) also leaves open a host of related questions. Does the Code limit remedies to those narrowly constructed to ensure full disclosure, or may broader remedies be granted? To what extent must a court, when shaping remedies, avoid interference with shareholder suffrage or state corporation laws? Of what significance is the defendant's consent? Must the SEC or a private plaintiff establish the traditional requirements of equity for the appointment of a receiver?

Although section 1819(l) and its comments do not resolve these questions, other provisions and comments do suggest some answers. The Code retains the disclosure orientation of the current law. In general, the purposes of the Code are to simplify, to eliminate duplicative regulation and to improve the scheme of investor protection "with the least possible interference to honest business."<sup>383</sup> Substantive changes have been

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382. *Id.* at 929-30.

383. 1 *id.* at xix, Reporter's Introduction (quoting President Roosevelt's message to Congress proposing the Securities Act of 1933, *see supra* note 181 and accompanying text). *See also* 1 ALI FED. SECS. CODE §§ 101 (setting forth the legislative findings of the need for the Code), 101(7) (stating that "this Code is essential . . . (B) to further the public interest and the protection of investors . . . without unnecessary regulation or undue interference with honest business . . .").



limited to technical matters.<sup>384</sup>

Accordingly, nothing in the Code authorizes the SEC to regulate corporate governance directly. Certain provisions dealing with fraud are unnecessarily vague on this point. The Code's definition of "fraudulent act" is tautological,<sup>385</sup> but does state that "[t]he existence of a fraudulent act is not precluded by the fact that it constitutes company mismanagement."<sup>386</sup> The comments to the Code as adopted by the ALI state cryptically that "[t]he words 'deceptive' and 'deceit' are deleted because they add nothing to 'fraudulent' and 'fraud'."<sup>387</sup> Apparently the drafters understood that deception is a necessary element of fraud, as it was traditionally, although some courts seemed to abandon that requirement under the securities laws prior to *Santa Fe Industries, Inc. v. Green*.<sup>388</sup> The Code's comments to both the definition of "fraudulent act" and the provision for civil liability for fraud state that they follow *Santa Fe*, which holds that mere unfairness in corporate management or even in securities transactions is not actionable under the Code.<sup>389</sup>

After discussions with the SEC, the Code's Reporter and a task force agreed to several changes, including an amendment of the definition of "fraudulent act" to cover deceit as well as fraud.<sup>390</sup> The amendment only makes clear that the Code is no narrower than existing law, however, and does not extend the Code's coverage to mere mismanagement or unfairness not involving deception.<sup>391</sup> Section 1819(a)(3) of the Code provides that in enforcement actions by the Commission, "fraudulent

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384. The Reporter stated that "[s]o far as substantive change is concerned, [the Code is limited] to what might loosely be called 'lawyer's law,' such as burdens of proof and measures of damages, and has avoided larger issues, which are 'political questions.'" 1 ALI FED. SECS. CODE at xxiv-xxv, Reporter's Introduction.

385. The Code provides that "'[f]raudulent act' includes an act, device, scheme, practice, or course of conduct that (i) is fraudulent or deceptive, or (ii) operates or would operate as a fraud or deceit." *Id.* § 202(61)(A) (Supp. I at 8).

386. *Id.* § 202(61)(E).

387. *Id.* § 202(61), comment 1(c).

388. *Santa Fe* held that a rule 10b-5 action requires an allegation of manipulation or deception. 430 U.S. 462, 473-74 (1977). See *supra* notes 228-40 and accompanying text.

389. 1 ALI FED. SECS. CODE § 202(61), comment 1(d) (1980); 2 *id.* § 1603, comments 2(y), 3(b).

390. 1 *Id.* § 202(61)(A) (Supp. I at 8).

391. The comment to the amendment states that it is intended "in order to avoid any argument of loss of coverage as compared with provisions like," *inter alia*, section 10(b) of the 1934 Act. *Id.* § 202(61)(A) (Supp. I at 9), comment.

act" includes an act "that is likely to defraud or deceive."<sup>392</sup> The purpose here seems to be the same as that of the amendment of the definition of fraudulent act. Thus the Code retains the securities laws' present insistence on deception as an element of fraud. The Code also imposes certain liabilities on fiduciaries, expressly including directors, but only for fraud, misrepresentation, or nondisclosure in connection with the purchase or sale of securities.<sup>393</sup> Breach of fiduciary duty alone does not violate the Code.

The Code codifies the holding of *Santa Fe* with respect to the residual power of state law. It provides that, with certain exceptions not here relevant, nothing in the Code "affects the application of State law . . . ."<sup>394</sup> This provision, combined with the limitation of the Code to regulation of disclosure, should keep courts wary of interpreting the Code, including the provision for ancillary relief, to interfere with state law.

The Code confers broad rulemaking powers on the Commission, but these powers must be exercised consistently with the purposes, conditions and restrictions of the Code.<sup>395</sup> It expressly denies the SEC power to "prescribe the qualifications of directors."<sup>396</sup> Because of the restrictions on the scope of the Code prescribed above, the SEC's rulemaking powers do not enable it to intrude directly on corporate governance.

The Code's express remedies demonstrate further that section 1819(I) does not authorize the restructuring of corporate boards as ancillary relief. In addition to retaining the Commission's power to seek injunctions, compliance orders and stop orders, to suspend trading, and to refer matters for criminal

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392. 2 *id.* § 1819(a)(3)(B).

393. *Id.* § 1709(a). Comment (6)(b) states that "1709(a) is entirely consistent with the decision not to overrule *Santa Fe* . . . . That is to say, the Code does not cross the line from 'fraud' to 'unfairness' . . . ."

394. *Id.* § 1904(j)(1). Comment 16(b) to this section states that "whether there is a 'conflict' will be decided by the courts" (emphasis in original), not by the Commission. *Id.* at 979, comment 16. Thus the SEC cannot by itself preempt state laws that would prevent the SEC from appointing or removing directors without shareholder action.

395. *Id.* §§ 1614, 1804(b).

396. *Id.* § 1805(g). This section negates any power of the Commission to "require every registrant to have a certain number of 'outside' directors . . . ." *Id.* § 1805(g), comment. The comment also notes that this "clause, however, has no bearing on the Commission's view that it has the authority to mandate audit committees of 'independent' directors in appropriate circumstances." *Id.* A comment in the first supplement to the Code further states that the clause also "carries no implication either way with respect to such matters as the Commission's authority . . . to take similar director-oriented action in the corporate governance area." *Id.* § 1805(g) (Supp. I at 44), comment.

prosecution,<sup>397</sup> the Code empowers the Commission to regulate the internal governance of certain corporations, but the types of corporations are specifically identified and are invariably part of the securities industry. Thus the Commission may in some cases obtain a trustee to conduct an ongoing business, the liquidation of a company, or the removal of an officer or trustee.<sup>398</sup> That the Code authorizes these remedies only as to the securities industry suggests that they were not intended to apply to general issuers.

All these factors tend to negate the availability of ancillary remedies that interfere with corporate governance. Nonetheless, the vague language of section 1819(l) and its comments might be read to justify such remedies. Accordingly, this provision should be amended so as to clarify its meaning and to avoid undesirable results. The factors to be considered in re-drafting section 1819(l) generally accord with those weighed in determining what the law of ancillary relief now is or should be. In the preceding Part of this Article, conclusions about what the law of ancillary relief is or should be were based largely on the purposes of the securities law—promoting full disclosure, preventing or remedying deception and manipulation in securities transactions, and assuring shareholder suffrage. Since the Code retains these purposes,<sup>399</sup> the current objection to judicial restructuring of corporate boards also compels amending the Code to prohibit these remedies: such restructuring is unnecessary to effective enforcement of the securities laws and intrudes improperly on shareholder suffrage and state control.

The Code should also bar appointment of special counsel without the corporation's consent. Although it would probably

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397. *Id.* §§ 1808(c) (order to file a required report or a corrected report), 1808(d) (stop orders), 1808(g) (suspend or terminate a stock exchange or over-the-counter listing), 1819(a) (actions for injunctions or to enforce compliance), 1821(h) (referrals to Attorney General for possible criminal prosecution). The Code also gives the Commission some new enforcement powers based on new substantive provisions of the Code. *See, e.g., id.* § 1808(a) (suspension of privilege of using summary prospectus).

398. *Id.* §§ 1809(a) (SEC may suspend or revoke registration of or place limitations on a securities professional), 1810-16 (administrative proceedings against self-regulatory organizations and their members, transfer agents, securities information processors, banks, affiliates of investment companies, and service companies), 1819(b) (appointment of trustee of clearing agency), 1819(f) (removal of officer of investment company for breach of fiduciary duty), 1819(g) (appointment of trustee of investment company), 1819(i) (liquidation of unit investment trust).

399. *See supra* notes 383-84 and accompanying text.

not violate the constitutional separation of powers doctrine for Congress to authorize such appointments,<sup>400</sup> the salutary purpose of that doctrine is slighted when the legislative function of granting enforcement powers is delegated to the courts and the SEC and the executive function of enforcing the law is delegated by the courts and the SEC to private citizens.<sup>401</sup> A corollary to the separation of powers principle is democratic control over the legislative and executive branches of government. This, too, is lost when the judiciary and the SEC can set the budget for securities enforcement through appointments of special counsel and when private citizens rather than by government employees in the executive branch conduct enforcement. To some extent these objections remain even when the corporation consents to the appointment, but it does not on balance seem objectionable that a corporation, pursuant to such a decree, should agree to such redress.<sup>402</sup>

Accordingly, section 1819(l)(1) should be amended by adding to the first sentence thereof the following proviso:

provided, the court shall not pursuant to this sentence order the appointment or removal of any director or officer of an issuer, nor require the revision of the board of directors or similar body of any issuer, nor, without the consent of the issuer, appoint counsel to investigate possible violations of this Code or to bring suit thereon on behalf of such issuer.

The Commission should be able to seek a receiver for an issuer in extreme circumstances, but to define these circumstances precisely by statute would require an exceedingly long provision, approaching a memorandum of law, and might still

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400. Although one purpose of such an appointment is to relieve the SEC of part of its enforcement burden, technically special counsel are empowered to sue on behalf of the corporation only, not the SEC. *See supra* text accompanying note 336. *See generally supra* notes 27, 336-43. Thus special counsel is not, strictly speaking, performing a governmental function. Although delegation of law-making power to private parties may create constitutional problems, *see* L. JAFFE & N. NATHANSON, *ADMINISTRATIVE LAW: CASES AND MATERIALS* 67-70 (4th ed. 1976), appointment of special counsel raises no such problems because, technically, no governmental powers are delegated. *But see infra* note 401 (appointment of special counsel goes beyond function of SEC).

401. "[T]he fundamental assumption behind the separation of powers is that because no branch of government can be trusted in its use of power, the power of each branch must be limited by some degree of functional specialization." Nagel, *supra* note 1, at 662-63 (citing *THE FEDERALIST* No. 51 (J. Madison)). Even though appointment of special counsel does not technically violate this principle, *see supra* note 400, it does permit the SEC and the courts to engage in activities which in spirit are beyond their "functional specialization."

402. *See supra* note 379 and accompanying text.

deprive the courts of necessary flexibility.<sup>403</sup> Perhaps the best approach is to refer briefly in the statute to the conditions for a receivership, but to leave the courts some flexibility and to expand on these conditions in a comment. Accordingly, the following should be added after the first sentence of section 1819(1) (1):

The court shall appoint a receiver pursuant to the preceding sentence only as permitted by the practice of equity, and only pending conclusion of the action and so long as necessary to preserve assets of the defendant to which investors may be entitled by reason of violations of this Code.

This provision loosens the traditional requirement of equity by extending the remedy to a plaintiff who has no legal interest in the defendants' property, since the SEC will always lack even a claim against this property while the investors on whose behalf the SEC is suing may have such a claim but will often lack the kind of existing legal interest which equity traditionally required.<sup>404</sup> It is hoped that, by referring to both the rules of equity and some specific conditions for receiverships, this formulation can leave courts sufficient flexibility without allowing them to abandon the traditional functions of receiverships.

The Code must also be changed to subordinate SEC actions to private suits when the SEC seeks recovery on behalf of investors. This modification stresses that the SEC is not a collection agency. If the Commission seeks to enjoin or otherwise to prevent future violations of the securities laws, it need not defer to private suits. Even when the objective is recovery for investors, the law may forbid private actions, or no private suit may have been brought or competently prosecuted. But if, for example, the SEC seeks restitution or rescission while a private suit for similar relief is being competently pursued, there is no reason not to stay the SEC's suit. If the private suit fails to procure adequate relief, the SEC can revive its action.<sup>405</sup> The Commission should welcome such stays because they help conserve its scarce enforcement resources. To provide for such stays, 1819(1) (1) should be amended by adding the following sentence:

An action by the Commission to recover money or property for inves-

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403. See generally *supra* notes 345-57 and accompanying text.

404. See *supra* note 358.

405. In general, a suit by the SEC may be treated like a second shareholder's derivative suit. See *supra* note 305. Of course, the Commission may also appear as *amicus curiae* in a private suit. See 3 L. LOSS, *supra* note 57, at 1935-36.

tors shall be stayed during the pendency of a private suit which in the opinion of the court will probably be adequate to obtain any such recovery to which investors are entitled.

The foregoing changes would improve the Code by clarifying the role of ancillary relief and retaining the remedies the Commission needs to discharge its duties while excluding it from areas not within its province and establishing proper priorities between SEC enforcement actions and private suits. Except for the limitations just suggested, the SEC should be able to pursue, and the courts to grant, any ancillary remedy appropriate in a given case.

The foregoing guidelines contradict much recent commentary advocating greater government involvement in corporate governance. Professor Christopher Stone, in particular, has argued that corporations are less susceptible than individuals to traditional legal sanctions. Neither fines nor individual liability of officers, he believes, adequately deters illegal behavior.<sup>406</sup> Accordingly, he advocates greater governmental regulation of corporate governance by means of a Federal Corporations Commission, especially when a corporation has seriously broken the law. Under Stone's doctrine, it might be wise to permit the SEC and the courts to restructure corporate boards as ancillary relief.

A short answer to Stone's thesis is that the Code's drafters have expressly eschewed major substantive changes in the securities laws and that it would therefore be inappropriate to use the Code to extend government regulation of corporate governance.<sup>407</sup> Perhaps the drafters' claim should not be taken at face value. They may have made that claim not only to

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406. In Stone's view, traditional legal sanctions tend to be ineffective when imposed on corporations because a corporation cannot be imprisoned and fines tend to be fairly small, they do not embarrass corporate managers as much as other financial losses (because fines can be ascribed to hazy laws and disobedient subordinates), they do not deter (because of uncertainty that a violation will be detected and punished), and they harm stockholders, who rarely deserve the harm. Both legislatures and courts tend to resist imposing large fines. Punishing individuals is also inadequate to alter corporate behavior because many offenses are committed by lower level employees who do not control the corporation; many offenses cannot be ascribed to specific individuals; higher officers cannot know everything lower employees do and are often deliberately screened from bad news; judges and juries hesitate to convict or punish individual officers; fines may be made up by indemnification or insurance; and criminal sanctions often lack accompanying peer group disapproval because corporate norms differ from legal norms. See C. STONE, *WHERE THE LAW ENDS* 39-69 (1975); Stone, *The Place of Enterprise Liability in the Control of Corporate Conduct*, 90 YALE L.J. 1, 14-35 (1980).

407. See *supra* note 384 and accompanying text.

dampen potential opposition to the Code but also to avert demands from all quarters for other major changes.

Although this is not an appropriate place for a sustained critique of Stone's arguments, it is fitting to note that Stone's premise that corporations are less susceptible than individuals to traditional legal sanctions is neither intuitively compelling nor empirically proved.<sup>408</sup> Even if one accepts Stone's premises about corporations and legal sanctions, it does not necessarily follow that greater government intrusion through an administrative agency is the best solution, especially with respect to SEC regulation of corporate governance.<sup>409</sup> There is

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408. Professor Galbraith and others have argued that corporate managers primarily look out for their own interests, not those of the corporation. J. GALBRAITH, *THE NEW INDUSTRIAL STATE* 171 (2d ed. 1971). See Donaldson, *Financial Goals: Management v. Stockholders*, 41 HARV. BUS. REV. 116 (May-June 1963). One would assume, therefore, that corporate managers would be especially careful not to break the law since most profits from violations benefit the many anonymous and ungrateful shareholders, while penalties for violations might well be imposed on the managers themselves. See J. GALBRAITH, *supra*, at 171 ("profit maximization as a goal requires that the individual member of the technostucture subordinate his personal pecuniary interest to that of the remote and unknown stockholder"). But see Werner, *Management, Stock Market and Corporate Reform: Berle and Means Reconsidered*, 77 COLUM. L. REV. 388, 388-89 (1977) (market pressures are so great that managers often feel compelled to break the law to increase profits). Stone's empirical support for his thesis does not rise above the anecdotal. *Where the Law Ends* is based on research of six case studies involving flagrant fraud, spectacular financial collapse or product defect, or questionable corporate political activity. C. STONE, *supra* note 406, at ix. It is highly doubtful that focusing on such aberrant cases can produce an analytical framework suitable to average public corporations. See Cohen, Book Review, 62 VA. L. REV. 259, 269 (1976) (review of *Where the Law Ends*).

409. While government regulation may prevent some undesirable corporate behavior, this benefit is not achieved without substantial cost. In particular, government regulation may discourage competition, innovation, and reasonable risk-taking, even when regulation is performed by an agency regulating a single industry so that the agency acquires considerable expertise with respect to that industry. This criticism has been leveled at many federal agencies, including the SEC. See R. KARMEL, *supra* note 140, *passim*; H. KRIPKE, *supra* note 140, *passim*. Although Stone's proposals differ radically from past and present regulatory schemes, so that Stone cannot be charged with most shortcomings of these schemes, the past failures of regulation counsel a cautious attitude toward proposals for more regulation. Some of Stone's proposals that have been tried have not been spectacularly successful. In particular, government appointed directors have been ineffective in recent cases and in the last century. See M. EISENBERG, *THE STRUCTURE OF THE CORPORATION* 167-69 (1976); DeMott, *supra* note 320, *passim*.

Although the SEC may possess expertise with respect to securities professionals, such as broker-dealers, investment companies and advisers, and securities exchanges, and although it may also be expert as to the corporate finance aspects of other businesses, such as financial reporting and accounting, it possesses no special expertise with respect to the general management of business outside the securities industry. Yet when the SEC and the courts bar individu-

no consensus as to any method of improving corporate governance substantially, nor even as to the goals of corporate governance other than the traditional goal of maximizing profits.<sup>410</sup>

Is the restructuring of corporate boards through ancillary relief more defensible than broader regulation of corporate governance by the SEC? Defenders of the SEC can argue that ancillary relief is granted only when a corporation has already violated the securities laws, thereby showing that the board has not been effective, and that in appropriate cases the SEC and the courts can improve compliance with the law and corporate governance generally by restructuring the board. A corporation's governance remains unregulated until its behavior demonstrates a need for regulation. This argument falters on the same objections that can be leveled against broader SEC regulation of corporate governance. The SEC has articulated no general goals of corporate governance that it seeks to achieve through ancillary relief, and it has no mandate from Congress to fashion such goals. The managerialist view voiced by some SEC officials is not only theoretically flawed but also has not commanded and could not now command the approval of Congress. This lack of any standards for corporate governance is fatal; without it there is no basis for measuring the effectiveness of the Commission's efforts.

If there lurks below the surface some unarticulated vision, or hidden agenda, for corporate governance, there is no evidence that the restructuring of corporate boards has furthered that vision. Even statistical evidence that corporations with boards restructured by the SEC had by some standard performed better than they had previously would not be terribly meaningful without comparison to some control group of corpo-

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als from serving as corporate managers, and suspend the shareholders' traditional right to elect directors, they necessarily regulate not only the corporation's financial disclosures but the conduct of its entire business. See *supra* text following note 312.

410. Although all but Marxists concede need for some devotion to profit, commentators disagree whether this should be the only goal of corporate activity, or whether corporations should also pursue social goals. See W. CARY & M. EISENBERG, *supra* note 299, at 219-23. Needless to say, commentators also disagree on what changes, if any, should be made in corporate governance. See *id.* at 223-26. Professor Kripke has written of the dangers to American business if the vision of managerialism embraced by some SEC officials were imposed on American corporations. Kripke, *supra* note 158, at 180-86. Even without accepting Professor Kripke's views entirely, however, one can well imagine the adverse consequences of replacing corporate managers responsible to shareholders and to market forces with managers responsible in some vaguely defined way to the SEC and to the courts.



rations that had been subjected to relief other than such restructuring. Moreover, if the object of ancillary relief is not improved corporate governance but only improved compliance with the securities laws, there is no evidence that restructuring corporate boards is more effective than other remedies. Indeed, logic suggests that other remedies might be more effective for that purpose.<sup>411</sup>

In sum, the assumptions that unsocial corporate behavior is a major problem and that increased government regulation of corporate governance is the solution are questionable. Even if such regulation were desirable, the SEC lacks the congressional mandate and the expertise to perform it. These problems apply equally to the regulation of corporate governance through ancillary relief. Accordingly, even if Congress considers substantive changes in connection with the ALI Federal Securities Code, policy considerations dictate that it forbid the SEC and the courts to restructure corporate boards as ancillary relief.

## VII. CONCLUSION

Although the Supreme Court and, as to some remedies, the federal courts generally have not yet grappled with the legal issues raised by ancillary relief in securities law, the Supreme Court's movement in recent years toward a narrower reading of the securities laws and a greater reluctance to infer statutory remedies suggests that the Court might well disapprove of at least some ancillary remedies that the SEC has obtained. As a result, there is now considerable uncertainty about the propriety of much ancillary relief in securities law. This Article has set forth the framework within which the problems of ancillary relief in securities law must be analyzed and has proposed some answers to these problems.

Similar problems have not arisen in other areas of administrative law because other administrative agencies generally have not sought such broad ancillary remedies as has the SEC. If the SEC continues to obtain such remedies, it would seem only a matter of time before other agencies try to do likewise. How should the courts handle such a development? To some extent the propriety of ancillary relief depends on the purposes of the legislation under which it is sought, and therefore the rules of ancillary relief must to some degree be specific to each

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411. See *supra* text accompanying notes 333-34.

administrative agency. Still, some general propositions may be stated. The availability of ancillary relief should depend in part on the statutory provisions for express remedies. An elaborate array of express remedies suggests that Congress thought through the question of remedies, granting those it wanted and withholding those it did not want. The traditions of equity are also relevant. It is likely that Congress intended the courts to grant remedies traditional to equity, but not remedies unknown to equity. Finally, defining what remedies are available for violations of federal statutes, especially remedies available to an administrative agency created by Congress, should be primarily a congressional function. Accordingly, the burden of proof should be on those advocating implied ancillary relief. For the same reason, solution of the problem of ancillary relief should come not from the courts, but from Congress. The best approach is for Congress to specify clearly the remedies available under federal legislation. Courts then would not grant remedies unless expressly provided for or contemplated by Congress. This approach would be the most consistent with the separation of powers and with democratic control of the law-making process.

